Principles of Economics

"Economics" is the Combination of two Latin words: "Oiko" + "Nomos" that means "System of a home". It explains that how can we manage the system of a home? It further applied on another Latin word "Polos" means "State". Hence, it expands the concept to a state that how can system of a state be managed efficiently?

At that time, economics was not given the status of a seperate subject. It was considered as a part of a subject "Political Economy" that is familiar as Political Science now a days. It was given the status of seperate subject in 1776 when first book of economics was written by Prof: Adam Smith. He was considered as "Father of Economics".

We will discuss two major branches of economics in your paper.

i- Microeconomics
ii- Macroeconomics

Short Questions:

1) Microeconomics:
It is a branch of economics in which small units of an economy are discussed. e.g. Demand, Supply, Consumer behaviour and firm theory etc.

2) Economy:
Economy means such organized set up of a country in which natural, human and artificial resources of a country are being best utilized to produce goods and services.

3) Economic System:
It means a such planned and co-ordinated mechanism of an economy by which available resources are best utilized. There are three main types of economic system:

i- Socialism / Centrally Controlled Economy
ii- Capitalism / Market Economy
iii- Islamic Economic System

4) Capitalism:
Capitalism means such economic System in which most economic decisions are ~~made~~ taken by market forces demand and supply. Govt. interferes only when it feels that individuals are not taken ~~b~~ in national interest. It is adopted by America, England and Europe.

5) Socialism:
It is such economic ~~a~~ system in which all economic decions are taken by central govt. or its designated department. It is followed by Russia, China and Cuba etc. Now a days, this economic system is not applied by any country in true spirit.

6) Islamic Economic System:
An economic system in which all economic decisions are finalized by the govt. according to teachings of Islam.

7) Basic Problems of Economy:
There are four basic problems of any economy:
i) What to produce?
ii) How much to be produced?
iii) How can be produced?
iv) For whom to be produced?

8) Schools of thoughts w.r.t. definition of Economics:
There are three Schools of thought:
i) Classical School of thought ⇒ Knowledge of Wealth
ii) Neo-classical b. of thought ⇒ Knowledge of material welfare
iii) Modern school of thought ⇒ knowledge of scarcity + choice

9) Adam Smith's Definition:
"It is a subject which deals with production of wealth, consumption of wealth, distribution of wealth and exchange of wealth." Name of his book is "Wealth of Nations"

10) Alferd Marshall's Definition:
"Economics is a subject in which those individual and joint efforts of humans are discussed which are very closely connected to the achievement of material welfare and its uses." Name of his book is "Principles of Economics".

11) Leonell Robbins's Definition:
Economics explains behaviour of a human that is adopted by him to solve the problem arised by the conflict of multiple wants and scarce resources that have alternative uses. His book's name is "Nature and Significance of Economic Science."

12) Causes of Economic Problem:
There are four causes of economic problem:
i- Unlimited wants/desires
ii- Difference in importance of wants
iii- Scare resources/Limited resources
iv- Resources have alternative uses.

13) Four Merits/Advantages of Marshall definition:
i- Priority to humans. v- Simple and Comprehensive
ii- Individual and joint human efforts are discussed.
iii- Modern economic issues like planning, development are discussed.
iv- End of economic activity is material welfare.

14) Four Demerits/Disadvantages of Marshall definition:
i- Services are ignored. v- Concept of Welfare is not clear.
ii- Isolated person's activities are not discussed.
iii- Limited the scope of economics. ~~[illegible]~~
iv- Un necessary distribution of material and non-material

15) Four Merits of Robbins definition:
i- More realistic
ii- Scientific and Comprehensive.
iii- Broader Scope
iv. A natural science

16) Four Demerits of Robbins definition:

i- Not neutral

ii- Social not physical science

iii- Normative Science.

iv. Modern economic issues are ignored.

17) Keynes's Definition of Economics.

Economics is a science which creates employment opportunities and increase GNP by making efficient utilization of scarce resources.

18) Utility:

It means a property of a thing by which an invidual can satisfy his any desire, e.g. water has property to fulfill our thirst desire, so it has utility for us.

19) Marginal Utility:

The change in total utility by utilizing an additional unit of a commodity is called marginal utility. It can be calculated as $MU = \frac{\Delta TU}{\Delta q}$

20) Zero Utility (Point of Saturation):

A such point during utilization of a commodity when our desire is fully satisfied and total utility can not increase further, is called zero utility or saturation point.

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) Initial Utility:
Utility achieved by the consumption of first unit of a commodity is called initial utility.

22) Total Utility:
It is the sum total of the utility derived from all the units of a commodity consumed.

23) Relationship between Total Utility and Marginal Utility:
There are three relations between TU and MU:
i- When TU is increasing, MU remains positive.
ii- When TU is maximum, MU is zero.
iii- When TU is falling, MU becomes negative.

24) Law of Diminishing Marginal Utility:
While other things remain constant, marginal utility becomes smaller and smaller due continuous consumption of a commodity.

25) Law of Equi Marginal Utility:/ Consumer's Equilibrium in utility
A consumer is said to be in equilibrium when he spends his limited income on the purchase of different commodities in such a way that marginal utility of last unit of each commodity becomes equal.

26) Equation of Consumer's Equilibrium w.r.t. Utility:
$$\text{Consumer's Equilibrium} = \frac{MU_a}{P_a} = \frac{MU_b}{P_b} = \cdots = \frac{MU_n}{P_n}$$

27) Indifference Curve:
An indifference curve represents such different combinations of two commodities which give the consumer same level of satisfaction. It's slope is
$$\text{slope of } IC = MRS_{x,y} = \frac{\Delta Y}{\Delta X}$$

28) Four Properties of Indifference Curves:
i- IC slopes downwards from left to right.
ii- These never intersect each other.
iii- Higher IC gives higher level of satisfaction.
iv- These are convex to the origin.

29) Budget Line/ Price Line of Consumer:
It shows the different combinations of two commodities x and y which a consumer can purchase while given the prices of commodities and income of consumer. It shows the purchasing power of the consumer. Its slope is:

$$BL \text{ of consumer} = \frac{P_x}{P_y}$$

30) Consumer's Equilibrium w.r.t. Indifference Curve:
A consumer is said to be in equilibrium at a point where highest possible IC touches to budget line. Relevant IC should also convex to the origin at this point.

31) Conditions of Consumer's Equilibrium:
i- Necessary Condition ⇒ Slope of IC = Slope of BL

$$\frac{MU_x}{MU_y} = \frac{P_x}{P_y}$$

ii- Sufficient condition:
IC must be convex to the origin at the equilibrium point.

32) Price Effect:
The effect on consumer's equilibrium due to change ~~of~~ in price of a commodity while the price of other commodity and income of consumer remain constant.

33) Income Effect:
The effect on consumer's equilibrium due to change in income of consumer while the prices of commodities remain constant.

34) Substitution Effect:
The effect on consumer's eq. due to change in price of one commodity while remaining at the same indifference curve. For this purpose, he has to substitute some units of required commodity with units of other commodity remaining at same satisfaction level.

35) Demand:

A specific quantity of a commodity that is purchased at a specific price is called demand. will to purchase & power to purchase.

36) Demand Function:

A mutual relationship between price of commodity and quantity demanded is known as demand function. It is written as:

$$Qd = f(P)$$

It is a decreasing function.

37) Law of Demand:

Demand of a commodity expands due to fall in price of commodity and contracts due to rise in price while other things remain constant. Its slope is negative

38) Elasticity of Demand / Price ~~of~~ Elasticity of Demand

The rate of change in demand due to change in price of a commodity is called elasticity of demand.

$$Ed = \frac{\Delta Qd}{\Delta P} \cdot \frac{P}{Qd} \text{ or } Ep = \frac{\Delta Qd}{\Delta P} \cdot \frac{P}{Qd}$$

39) Income Elasticity of Demand:

The Rate of change in demand of a commodity due to change in income of consumer is called income elasticity of demand.

$$Ey = \frac{\Delta Qd}{\Delta Y} \cdot \frac{Y}{Qd}$$

40) Cross Elasticity of Demand:

The rate of change in demand of b commodity due to change in price of a commodity is called cross elasticity of demand.

$$Ec = \frac{\Delta Qb}{\Delta Pa} \cdot \frac{Pa}{Qb}$$

It is related to substitutes and complements. Income elasticity of substitutes is positive and it is negative in case of complements.

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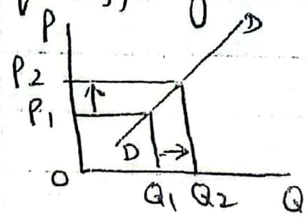
41) Giffin Goods:

These commodities are introduced by a British Mathematician Sir Robert Giffin. These are such commodities which are against law of demand. Demand of such commodities increases due to increase in price and decreases due to fall in price. e.g. Jawar or Bajra in food items.

42) Exceptional Demand Curve:

This curve shows positive relationship between price and demand. Demand curve of Giffin goods is exceptional demand curve.



43) Expansion and Contraction of Demand:

When the reason of demand is change in price of commodity itself, it is called expansion and contraction of demand. Demand curve does not change in this case.

44) Increase and Decrease in Demand:

When demand changes due to change in any other factor like weather, fashion or price of substitute, it is known as increase or decrease in demand. A new demand curve is derived in this case.

45) Write names of methods of measurement of elasticity of demand:

~~Therefore~~ There are four methods of measurement of demand elasticity:

i- Unitary Method or Total Outlay Method.
ii - Flux Method or Percentage Method
iii- Formula Method
iv - Geometric Method Total Expenditure method.

46) Supply:

A specific quantity of a commodity that is sold at a specific price in the market is called supply.

47) Supply Function:

A mutual relationship between price and quantity of a commodity sold in market, is called supply function. It is an incrasing function.

$Qs = f(P)$

48) Law of Supply:

Supply of a commodity expands due to rise in price and contracts due to fall in price while other things remain constant.

49) Stock and Supply:

Total quantity of a commodity that are kept by producer in reserves is called stock while supply means a specific quantity that is sold in market at a particular price is known as supply.

50) Reserve Price:

It is the minimum acceptable price at which the seller is willing to sell the commodity. He can refuse to sell it below this price.

51) Price Determination:/ Market Equilibrium

Price of a commodity is determined at a point where demand becomes equal to supply.

$$Qd = Qs$$

52) Equilibrium Price:

A price at which market equilibrium establishes is called equilibrium price

53) Equilibrium Quantity:

The quantity at which market equilibrium establishes is called equilibrium quantity.

54) Short Run and Long Run:

Short run means such small time of period in which producer can increase supply to a certain limit whereas long run is such a long period of time in which a producer can increase supply upto a level which he desires.

55) Perfect Competition:

A specific situation of market when following conditions are fulfilled is called perfect competition or competitive market.

i- Homogeneity of Product ii- Large Number Buyers and Sellers
iii- Free Entry and Exit iv- Elasticity of supply of Production Factors
v- Perfect knowledge of the Market.

56) Production Function:

Mutual relationship between quantity of production and units of factors is called production function.

$$Q = f(L, K, N, O)$$

57) Monopoly:

It is a market situation when a single producer or organization has complete authority to produce and sell of commodity or service, is called monopoly. e.g.

WAPDA has complete authority to sell electricity in country. There is no close substitute available in the market.

58) Law of Increasing Returns:

In any production process if the marginal productivity of variable factor, when it is combined with fixed factor, is increasing then this situation leads to the law of increasing returns. This law mostly applies in industrial sector.

59) Law of Decreasing Returns:

In any production process if the marginal productivity of variable factor, when it is combined with fixed factor, is decreasing ~~returns~~ then this situation leads to the law of decreasing returns. This law is applicable on every business. But the sectors which are very close to the nature like agriculture sector are directly and soon effected by this law.

60) Law of Variable Proportions:

This law explains that if we put the units of variabl factor like labour on the fixed factor like land, then every ~~unit~~ additional unit of variable factor increases the production more than before. But after a point, the proportion of this increment going to decrease consequently, the total production start decreasing after reaching its peak.

61) Total Cost:

It includes all types of expenses faced by the firm while producing a specific quantity of commodity like rent, wages, price of machines, raw material, publicity etc.

It can be divided into two types:

Total Cost = Fixed Cost + Variable Cost. ($TC = FC + VC$)

62) Fixed Cost.

It is also called as 'Indirect Cost' or 'Supplementary Cost'. It is permanent in nature and remains constant in short run. Firm bears this cost even on zero production. It is price of land, rent, wages of permanent staff,

63) Variable Cost:

It is also known as 'Direct Cost' or 'Prime Cost'. It changes with the change in units of output. It increases with increase in production and vice versa. It is price of raw material, wages of workers, transportation cost, sales tax etc.

64) Average Cost:

It is cost of average per unit output. It is obtained by dividing total cost over units of output.

$$AC = \frac{TC}{Q}$$

65) Average Fixed Cost:

When fixed cost is divided by total units of output.

$$AFC = \frac{FC}{Q}$$

66) Average Variable Cost: obtained by

Average variable cost is dividing variable cost over output units.

$$AVC = \frac{VC}{Q}$$

67) Marginal Cost.

The change in total cost due to production of one additional unit of output is called marginal cost.

$$MC = \frac{\text{Change in TC}}{\text{Change in Q}} = \frac{\Delta TC}{\Delta Q} = \frac{dTC}{dQ}$$

68) Total Revenue:

It is the total amount obtained by a fi[rm] after selling its total output produced during a speci[fic] time period. Hence $TR = P.Q$

69) Average Revenue:

Average revenue is obtained by dividing t[otal] revenue over quantity of production. It is also called per un[it] product. It is actually the price recieved per unit product

$AR = \frac{TR}{Q} \Rightarrow$ As $P = AR$ $\because TR = AR.Q$ or $TR = P.Q$

70) Marginal Revenue:

The change in total revenue by selling an additional unit of product.

$MR = \frac{\Delta TR}{\Delta Q} = \frac{dTR}{dQ}$

71) Short Run:

It means a such small period in which a producer can bring about a restrict increase in supply. He can increase production to a certain limit e.g. an additional unit shift can be started or stock can be provided in market.

72) Long Run:

A such long period of time during which a firm can change its production to a level that it desires. A firm can even install a new production unit during this time perio[d]

73) Monopolistic Competition:

It is a market situation that is the combination of perfect competition and monopoly. A market situati[on] in which many monopolists are competing with each other on the basis of product differenciation. Present market ~~si~~ situation is a clear example of monopolistic competition.

74) Conditions of Firm's Equilibrium:

There are two conditions of firms equilibrium:

i) $MR = MC$ (Necessary Condition)

ii) MC intersects MR curve from below when rising i.e.

Slope of $MC >$ Slope of MR (Sufficient Condition)

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Short Questions:

1) National Income:

Aggregate of all goods and services produced in an economy on market prices during the period of one year after substracting depreciation allowances and inderect taxes is called national income. National income = N.N.P. – Indirect Taxes.

2) Macroeconomics:

It is a branch of economics in which aggregates of an economy are discussed e.g. national income, investment, economic planning etc.

3) Concepts of National Income:

Following are the concepts of national income:

i- Gross National Product
ii- Net National Product.
iii- National Income
iv- Gross Domestic Product
v- Personal Income
vi- Disposable Personal Income
vii- Per capita income

4) Gross National Product:

Aggregate of all goods and services on market prices during period of one year is called gross national product. It also includes the income of foreign sector.

5) Net National Product:

Aggregate of all goods and services on market prices during period of one year after subtracting depreciation allowances is called net national product.

N.N.P. = G.N.P. – D.A.

6) Gross Domestic Product:

Aggregate of all goods and services on market prices during period of one year by utilizing domestic/internal resources only is called gross domestic product.

7) Per Capita Income:

It is calculated by dividing total national income over total population.

$$P.C.I = \frac{\text{National Income}}{\text{Population}}$$

8) Depreciation Allowances:

The expenditures made on wear and tear of machinery and equipment during period of one year is called depreciation allowances.

9) Disposable Personal Income:

The income in the possession of a man after the payment of direct taxes is called disposable personal income.

Disposable Personal Income = Personal Income - Direct Taxes

10) Methods to measure National Income:

Three methods to measure national income:

i- Product Method or Output Method

ii- Income Method

iii- Expenditure Method

11) Circular Flow of National Income:

In capitalistic system, economy is divided into two sectors: Households and Firms. Households provide their services to firms to produce goods and services that are subsequently provide to households. This circle continues. Firms pay wages to factor services as rewards that are further utilized to purchase goods and services from firms.

12) Types of Resources:

There are three types of resources:

i- Natural Resources.

ii- Man-made / Artificial Resources.

iii- Human Resources.

13) Equilibrium of National Income:

There are two methods to determine equilibrium of national income.

i- Agg Demand = Agg Supply => AD = AS

ii- Saving = Investment => S = I

Shafiq

14) Inflation:

When prices tend to rise more rapidly than the production of goods and services, it is called inflation. OR

"A typical situation of an economy when too much Chases too few things."

15). Causes of Inflation:

i- Increase in quantity of money.
ii- Increase in demand for goods
iii- Increase in cost of production.
iv- Development expenditure.
v- Rapid Increase in Population

16). Measures to Control Inflation:

i - Increase in Bank Rate
ii - Open Market Operation
iii - Reduction in Govt. Expenditure
iv - Increase in Taxes
v - Population Control
vi - Price Control Policy.

17) Deflation:

A situation in which quantity of money is less than the quantity of goods and services.

⟹ [Causes and Measures are the same as inflation but on opposite side.]

18) Unemployment:

It means such situation of economy when manpower is available for work but there is no opportunity to work. It is called unemployment. It can be frictional, seasonal, cyclical and disguised unemployment.

19) Disguised Unemployment:

It is a type of unemployment in which people are busy in working but they are facing unemployment in the sense that there will be no decrease in production of relevant sector if they are shifted to other sector of economy. It is about 20% to 30% in agriculture sector of Pakistan.

20) Consumption Function:

A mutual relationship between consumption and income is called consumption function. It is an increasing function.

$$C = f(Y)$$

Consumption increases with increase in income and vice versa.

21) Saving Function:

A mutual relationship between saving and income is known as saving function. It is an increasing function.

$$S = f(Y)$$

saving increases as income increases and vice versa.

22) Average Propensity to Consumption:- (APC)

The ratio between consumption and income is called average propensity to consume. If income is 500 and consumption is 200, Then A.P.C. is

$$APC = \frac{C}{Y} = \frac{200}{500} = 0.4$$

A.P.C. is always less than 1 and greater than zero.

$$0 < APC < 1$$

23) Average Propensity to Save: (APS)

The ratio between saving and income is called average propensity to save. If income is 500 and saving is 300, then APS is:

$$APS = \frac{S}{Y} = \frac{300}{500} = 0.6$$

APS is also always less than one and greater than zero.

$$0 < APS < 1$$

24) Marginal Propensity to Consume: (MPC)

The ratio between change in consumption (ΔC) to change in income (ΔY) is called marginal propensity to consume.

$$MPC = \frac{\Delta C}{\Delta Y} \Rightarrow 0 < MPC < 1$$

25) Marginal Propensity to Save: (MPS)

The ratio between change in saving (ΔS) to change in income (ΔY) is called marginal propensity to save.

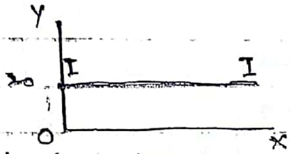
$$MPS = \frac{\Delta S}{\Delta Y} \Rightarrow 0 < MPS < 1$$

26) Investment:

It means to increase real assets of capital. For example: construction of a new building, a new power station or a road, dam, etc.

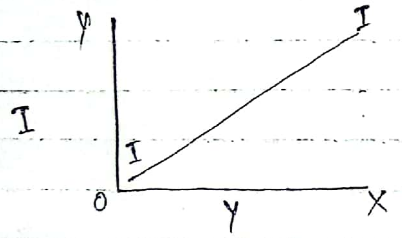
27) Autonomous Investment:

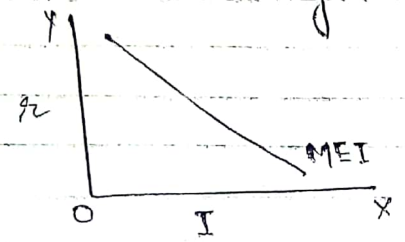
It is such type of investment that is not related to any demand. It is normally from govt. sector. Private sector never starts this investment because the demand of product is zero. It requires a fixed amount that is allocated by govt. in its annual budget.



28) Induced Investment:

This type of investment is induced by income or rate of interest. It varies with level of income and interest rate. Investment and income has positive relationship while investment and interest rate has negative relationship.

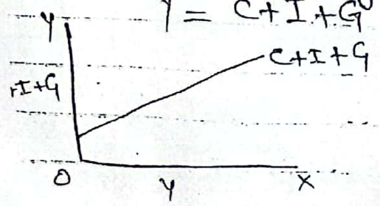




29). Aggregate Demand: (AD)

Aggregate of all types of expenditure in an economy at a specific time is called aggregate demand. e.g. in three sector economy:

$Y = C+I+G \implies$ C = Consumption expenditure
I = Investment "
G = Govt. Expenditure



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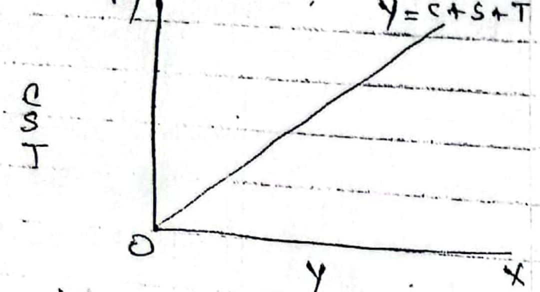
30) Aggregate Supply: (AS)

Aggregate of production in an economy a specific time is called agg. supply as all types of expenditures are used to produce goods and services.



$Y = C + S + T \Rightarrow$

C = Consumption

S = Saving.

T = Taxes.

31) Monetary Policy:

All measures taken by central bank of a country to regulate quantity of money / money supply is called monetary policy.

32) Tools of Monetary Policy:

A) Quantitative Tools/Measures: Bank Rate Policy.
Open Market Operation
Change in Reserve Ratio
Credit Rationing

B) Qualitative Tools/Measures: Moral Persuation
Direct Action
Publicity
Change in Marginal Requirement.
Regulation of Consumer's Credit

33) Fiscal Policy:

All revenue generating and expenditure making activities of central govt. is called fiscal policy. In other words; federal budget is the another name of fiscal policy.

34) Public Finance:

It is that branch of economics which studies revenue and expenditures of govt. institutions, their relationship and financial administration.

35) Components of Public Finance:
i- Public Revenue
ii- Public Expenditure
iii- Public Debt.

46) Canons / Principles of Taxation:
i- Canon of Equality — ii- Canon of Certainty
iii- Canon of Economy — iv- Canon of Convenience.
v- Canon of Simplicity — vi- Canon of Productivity.

47) Sources of Public Revenue:
i- Taxes — ii- Fee
iii- Price — iv- Fines
v- Govt. Property — vi- Local Rate

48) Heads of Public Expenditure:
i- Istalment and Interest on Loans — ii- Defence
iii- Police — iv- Civil Administration
v- Courts — vi- Public Health / Education.

49) Balance of Payments: (BOP)
It is a systematic record of all economic transactions (visible & invisible) between reporting country with the rest of the world over a specified period of time.

50) Balance of Trade: (BOT)
It is a norrow concept as compared to balance of payments. It is a systematic ~~rag~~ record of all economic transactions of visible items only i.e. (exports and imports).

51) Items of BOP:
i- Services of Banks, Insurance Companies & Shipping Companies.
ii- Tourism
iii- Study abroad iv- Medical Treatment v- Foreign Aid

52) Causes of Unfavourable BOP:
i- Increase in imports — ii- Decrease in Exports
iii- Inflation — iv- Technology Progress
v- Unfavourable TOT — vi- Foreign Loans.

53) Measures to correct BOP:

i- Improve in BOT
ii- Decrease in Quantity of M...
iii- Foreign Exchange Control
iv- Population Control
v- Devaluation
vi- Import substitute industry.

Q.1)

54) Direct Tax:

It is a tax which is imposed on the person and it is payable by the same person. This tax is not transferable to other persons. e.g. income tax, property tax and wealth tax.

55) Indirect Tax:

It is a tax which is imposed on one person but may be shifted to other persons. So, the final burden of the tax on consumers because these taxes are included in the price of products. e.g. sales tax, custom duty and central excise duty.

56) Multiplier:

It shows a relationship between initial increase in investment and the resulting increase in national income. Thus, it explains the relationship between increase in investment and the resulting increase in income. It can be calculated as:

$$k = \frac{1}{1-MPC} \quad \text{or} \quad k = \frac{1}{MPS}$$

57) Accelerator Principle:

It shows an economic concept that represents a connection between change in consumption patterns and corresponding increase in capital investment.

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Money

PERFECT COMPETITION.

Q.1) Define market price?

It is temporary price that is related to day to day market. It is settled by supply and demand within a day. It is of perishable commodities and is also called short period price.

Q.2) Define normal price.

It is also called long run price. It is settled by stable equilibrium of demand and supply. It is associated normally with durable commodities.

Q.3) Write types of markets according to time period.

i- Day to day market.
ii- Short period market
iii- Long period market.

Q.4) What are types of market according to nature of competition.

i- Perfect competition
ii- Monopoly.
iii- Duopoly.
iv- Oligopoly.
v- Monopolistic Competition.

Q.5) Define perfect competition.

A market where following five conditions/assumptions are fulfilled is known as perfect competition.

i- Homogeneity of the product.
ii- Large number of buyers and sellers.
iii- Free entry and exit.
iv- Elastic supply of factors of production.
v- Perfect knowledge of market.

Q. 6) Define monopoly.

Monopoly is a market where a single person or organization (firm) has fully control over production or sale of a good or service. There is no close substitute available in the market. e.g WAPDA or Pak Railway

Q.7) What is monopolistic competition?

A such market when there are many sellers are competing with each other on the basis of product differentiation. Present market is a clear example of monopolistic competition.

Q.8) Write the conditions of firm's equilibrium.

There are two conditions of firm's equilibrium:

i- Marginal Cost (MC) = Marginal Revenue (MR)

ii- MC curve must intersect MR curve from below.

Q.9) How many types of firm's equilibrium under perfect competition in short run?

i- Super normal profit.

ii- Normal profit.

iii- Normal Loss.

iv- Abnormal Loss / Shut down point.

Q.10) Define shut down or close down point of a firm.

It is a situation of firm's equilibrium in which price is equal to firm's average variable cost. It means only variable costs are covered and firm's loss is equal to total fixed costs.

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1. Elasticity of Demand

Q.1) Define elasticity of demand.

Rate of change in demand due to change in price of a good is called elasticity of demand. It is denoted by Ed.

Q.2) Write the formula of elasticity of demand.

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

Q.3) What is arc elasticity of demand.

When there is major change in demand and price of a good and we have to measure elasticity between two distinct points of a demand curve is called arc elasticity of demand. It's formula is

$$Ed = \frac{Q_1 - Q_2}{Q_1 + Q_2} \div \frac{P_1 - P_2}{P_1 + P_2}$$

Q.4) Define point elasticity of demand.

When there is very minor changes in demand and price of a good and two points on demand curve are so close to each other. It is called point elasticity of demand and its formula is

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

Q.5) What is cross elasticity of demand?

The rate of change in demand of b commodity due to change in price of a commodity is called cross elasticity of demand. It is measured by

$$Ec = \frac{\Delta Q_b}{\Delta P_a} \cdot \frac{P_a}{Q_b}$$

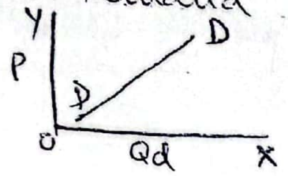
Q.6) What do we mean by income elasticity of demand.

The rate of change in demand of a commodity due to change in income of consumer is called income elasticity of demand. It is measured by

$$Ey = \frac{\Delta Q}{\Delta Y} \cdot \frac{Y}{Q}$$

Q.7) What is exceptional demand curve?

When demand increases due to rise in price of a commodity and decreases due to fall in price. The resultant curve is called exceptional demand curve.



SUPPLY

Q.1) What is supply?

A specific quantity of a commodity that is sold at a specific price is called supply.

Q.2) Define supply function.

A mutual relationship between supply and price of a good is called supply function. i.e.

$Qs = f(P)$ (an increasing function)

Q.3) Differentiate between stock and supply.

Total quantity of a commodity that is kept by producer is called stock and a specific quantity that is provided by producer in market at a specific price is called supply.

Q.4) Define law of supply.

While other things remaining constant, quantity supplied increases due to rise in price of a good and supply decreases due to fall in price of a good.

Q.5) Write names of types of supply w.r.t. time period.

i- Fixed Supply
ii- Short period Supply.
iii- Long period Supply.

Q.6) What is reserve price?

It is the minimum acceptable price at which the seller is willing to sell the commodity.

Q.7) Define composite supply.

Sometimes there are different sources of supply of a good. The sum total of supply from all the available resources, we get composite supply. e.g. meat from sheep, goat, chicken, fish etc.

Q.8) What do we mean by joint supply?

Some goods are jointly produced. Thus an increase in supply of a good results a rise in supply of the other good and vice versa. e.g. meat with wool.

Q.9) What is competitive supply?

Supply of some goods compete with each other when there are more than one uses. If supply is increased in one use, it's supply for the other use will become less. e.g. supply of electricity for domestic, commercial or industrial use.

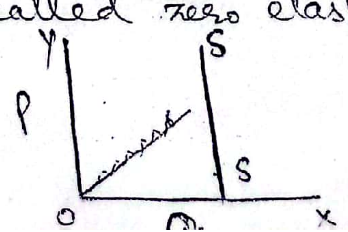
Q.10) Define elasticity of supply.

The rate of change in supply of a good due to change in its price is called elasticity of demand.

$$E_s = \frac{\Delta Q}{\Delta P} \cdot \frac{P}{Q}$$

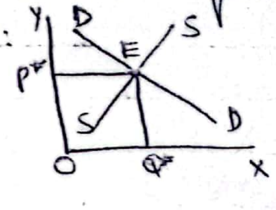
Q.11) What is zero elasticity of demand?

If there is no change in supply of a good due to change in price is called zero elasticity of demand. Its curve is



Q.12) What is market equilibrium or demand and supply equilibrium?

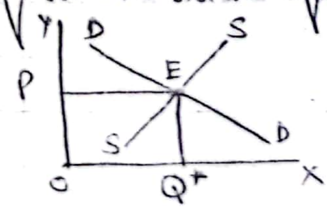
Market equilibrium establishes at a point where demand and supply become equal to each other. It is denoted as:



$Qd = Qs.$ (point E)

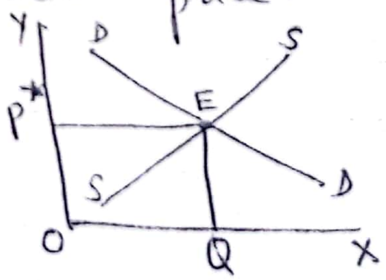
Q.13) What is equilibrium price?

The quantity at equilibrium point of market is known as equilibrium quantity. i.e. OQ^* in diagram.



Q.14) Define equilibrium price.

The price at equilibrium point of market is called equilibrium price. i.e OP^*



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DEMAND

Q.1) What are essentials of demand?
There are two essentials of demand:
i) Will/Desire to purchas.
ii) Ability to purchase.

Q.2) Define demand.
A specific quantity of a commodity that is purchased at a specific price is called demand.

Q.3) What is demand function?
It means a mutual relationship between price and demand of a commodity. It is written as
$$Qd = f(P)$$
It is a decreasing function. That shows an inverse relationship between both variables.

Q.4) Define law of demand.
while Other things remaining the same, when a price of a commodity increases, its demand decreases and when price of a commodity decreases, its demand increases.

Q.5) Define derived demand.
Demand of some commodity is not direct. It is derived from the demand of some other commodity. e.g. demand for a house is direct but for the construction of that house demand for bricks, cement, iron, wood, labour etc.

Q.6) What is joint demand?
The satisfaction of some human want depends upon the simultaneous demand for more than one good i.e such as car and petrol, pen and ink etc. Such goods have joint demand.

BUSINESS ECONOMICS

Short Question answers:

Q.1) Define business economics.

Business economics is a field of applied economics that studies the financial, organizational, market related and environmental issues faced by corporations. It includes subjects such as concept of scarcity, produc factors, distribution and consumption.

Q.2) What is the importance of business economics?

It is important because it helps people understand how a variety of factors work with and against each other to control how resources such as labor and capital get used, and how inflation, supply, demand, interest rates and other factors determine how much you pay for goods and services.

Q.3) What is scope of business economics?

It covers most of the problems that a manager or businessman faces. Hence, the scope of business economics is wider. Since, a firm can face internal/operational as well as external/environmental issues, there are different economic theories applicable to them.

Q.4) Write down main features of business economics.

i) Business economics is micro in nature.
ii) It provides basis of Theory of Markets and Private Enterprises.
iii) Pragmatic in its approach.
iv) Normative in nature.
v) Macro Analysis.

Q.5) Differentiate between business and economics.

Business and economics go side by side as business offer products and services that generate economic output e.g. business sell goods and services to consumers whereas economics determines the supply and demand of such products in an economy.

Q.6.) What is the role of business economist?

i) To bring reasonable profit to the company.
ii) To study internal and external factors influencing the business.
iii) To make accurate forecast.
iv) To establish and maintain contact with individual and data resources.
v) To keep the management well informed of all possible economic trends.

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It is a field of applied economics ~~that studies the financial organizations~~ in which we apply different economic theories about cost, demand, supply, price etc to analyze business. It is also an important tool of decision making and helps in the management of the firms.