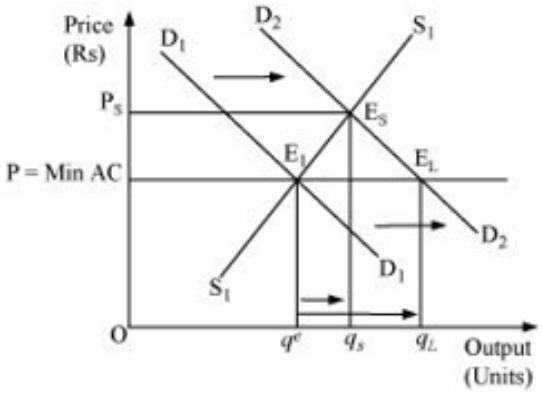
Q20. Can you think of any commodity on which price ceiling is imposed in India? What may be the consequence of price-ceiling?
Ans: In India, there are many goods on which government has imposed price ceiling, in order to keep them available within the reach of the BPL (below poverty lime) people. These goods are kerosene, sugar, wheat, rice, etc.
The following are the consequences of price ceiling:
i) Excess demand – Due to artificially imposed price, cutting lower than the equilibrium price leads to the emergence of the problem of excess demand.
ii) Fixed Quota – Each consumer gets a fixed quantity of good (as per the quota). The quantity often falls short of meeting the individual's requirements. This further leads to the problem of shortage and the consumer remains unsatisfied.
iii) Inferior goods – Often it has been found that the goods that are rationed are usually inferior goods and are adulterated.
iv) Black marketing – The needs of a consumer remain unfulfilled as per the quota laid by the government. Consequently, some of the unsatisfied consumers get ready to pay a higher price for the additional quantity. This leads to a black-marketing and artificial shortage in the market.

Q21. A shift in demand curve has a larger effect on price and smaller effect on quantity when the number of firms is fixed compared to the situation when free entry and exist is permitted. Explain.

Ans:



The above figure depicts both the cases when the number of firms is fixed (in short run) and when the number of firms is not fixed (in long run). P = min AC represents the long run price line; D_1D_1 and D_2D_2 represents the demand in the short run and the long run respectively. The point E1 represents the initial equilibrium, where the demand and the supply intersect each other. Let us suppose that the demand curve shifts, assuming that the number of firms is fixed. Now, the new equilibrium will be at E_s (as it is short run equilibrium), where the supply curve and the demand curve D_2D_2 intersect each other. The equilibrium price is P_s and equilibrium quantity is q_s.

On the other hand, under the assumption of free entry and exit, an increase in demand will shift the demand curve rightwards to D_2D_2. The new equilibrium will be at E_2 (as it is a long run equilibrium) with the equilibrium price P = min AC and equilibrium quantity q_L.

Therefore, on comparing both the cases, we find that when the firms are given the freedom of entry and exit, the equilibrium price remains the same. The price is lower than that of the short run equilibrium price (P_s); whereas, the long run equilibrium quantity (q_L) is more than that of the short run equilibrium quantity (q_s).

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