

Chapter 1-

Nature and Scope of Business Economics

1. Economics originated from **Greek work** ''*Oikonomia*'. *Oiko*-'House' & *Nomia*,- 'Management'.
2. Till 19th century, Economics was also known as 'Political Economy'
3. Basic Economics problem **unlimited wants**, and **Scarce resources**.
4. Resources shall be allocated to their **highest valued uses**.
5. Economics is study of **transformation of the scarce resources** into G&S to satisfy the most important of our infinite wants
6. The book named '**An Inquiry into the Nature and Causes of the Wealth of Nations**' (1776), by **Adam Smith** is considered as the first modern work of Economics.
7. **Decision making** - process of **selecting an appropriate alternative** that will provide the most efficient means of attaining a desired end, **from two or more alternative** courses of action".
8. **Decision making** arises only if there is choice available. No alternatives no decision making- e.g.-Continue or shut down decision, New Product, Make or buy, Marketing
9. **Joel Dean** defined Business Economics as the use of economic analysis to make business decisions involving the best use of an **organization's scarce resources**.-
10. Business Economics is referred as **Managerial Economics**, generally refers to the integration of economic theory with business practice.
11. **Economic theories are hypothetical** and **simplicistic** in since based on simplifying assumptions.
12. Business Economics enables application of economic logic and analytical tools to **bridge the gap** between theory and practice.
13. Business Economics is not only valuable to business decision makers, but also useful for managers of **'not-for-profit' organizations**

14. Difference between Micro and Macro Economics

Micro Economics	Macro Economics
Greek work 'Mikros' which means 'Small'	Greek work "Makros" which means 'large'
"Study of particular firm, particular household, individual price, wages, income, individual industries, particular commodities"- Prof. Boulding	"Macro Economics examines the Forest and not the Trees. Large aggregates "- Prof. Mc. Connel

Behavior of individual firm or industry	Overall economic phenomena
It is also called as „ Price Theory ”	It is also called as „ Income Theory ”

15. **The Nature of Business Economics is described as under-**

- (a) **Business Economics is a Science-** Explains cause and effect relationships.
- (b) **Business Economics is an art** -application of rules and principles
- (c) **Micro Economics based and Macro Analysis based**
- (d) **Analysis from Private Enterprises Economy viewpoint**
- (e) **Inter-Disciplinary-** Integrates the tools of decision sciences such as
- (f) **Mathematics, Statistics and Econometrics with Economic.**

16. **Normative and positive -**

Positive Economics or Pure economics	Normative Economics
It is based on facts and there is no point of ambiguity or second view	It tells us about how the things should be.
Descriptive in nature & It states 'what is'	Prescriptive in nature & describes 'what ought to be'.
It explains cause & effect relationship and there will be no value judgments/suggestions.	It passes value judgments /suggestions and offers advice.
It is based on past data and can be checked with data	Cannot be verified because it is opinion based and not fact based
No Matter of debate	Matter of Debate
According to Robbins , Economics is neutral between ends.	It is based on welfare economics - (Marshall & Pigou) Complete neutrality between ends is, however, neither feasible nor desirable.

17. **Scope of Business Economics**

- a. **Microeconomics applied to operational or internal Issues-** issues within the organization and fall within the purview and control of the management.

1. Demand Analysis	2. Demand Forecasting	3. Cost analysis
4. Theory of Capital and Investment Decisions	5. and Uncertainty Analysis	6. Market Structure and Pricing Policies
7. Resource Allocation	8. Production analysis	9. Inventory Management
10. Profit analysis		

b. Macroeconomics applied to environmental or external issues- *issues out of preview of an organization* The major macro-economic factors relate to

- 1) The type of economic system.
- 2) Stage of business cycle.
- 3) The general trends in national income, employment, prices, saving and investment.
- 4) Government's economic policies like industrial policy, competition policy, monetary and fiscal policy, price policy, foreign trade policy and globalization policies.
- 5) Working of financial sector and capital market.
- 6) Socio-economic organizations like trade unions, producer and consumer unions and cooperatives.
- 7) Social and political environment.

Central Economic Problems

1. All countries, without exceptions, face the problem of scarcity because their resources are **limited** and these resources have **alternative uses**.
2. If a resource has only a single use, then also the economic problem would not arise.
3. The central economic problem is further divided into four basic economic problems.
 - a) **What to produce? Which goods and in what quantities**
 - b) **How to Produce? Method of production**, (labour- intensive or capital - intensive)
 - c) **For whom to produce?** How the G&S should be distributed among members of the society. Also **shares of different people** in the national product.
 - d) **What provisions (if any) are to be made for economic growth? -saving and investment**

4. Understanding different types of Economies

Particular	Capitalist economy	Socialist economy	Mixed Economy
Also Known as	Free market economy or laissez-faire economy	Karl Marx and Frederic Engels in their work „The Communist Manifesto“ published in 1848	Depends on both markets and govt.

Most imp Feature	Private Ownership	Collective Ownership/ Public ownership	<i>Include the best features of both the controlled economy and the market economy while excluding the demerits of both.</i>
Other points	Private property is the mainstay. Profit motive is its driving force		
How CEP are resolved	Impersonal forces of market demand and supply or the price mechanism		
What To produce	Decided by consumers	Decided by CPE	
How to produce	Cost of production minimum. Labor or capital Intensive		
For Whom to produce	Those who have buying capacity		
What provision are to be made for economic growth?	Depends upon level of interest rate for consumer and rate of return in Market for business firm		

5. Characteristics of each type of economy

Capitalist economy	Socialist economy	Mixed Economy
<ul style="list-style-type: none"> a. Right to private property b. Freedom of enterprise c. Freedom of economic choice d. Profit Motive e. Consumer Sovereignty f. Competition g. Absence of 	<ul style="list-style-type: none"> a. Collective Ownership of means of production by state however, small farms, workshops & trading firms which may remain in private hands. b. Profit- motive and self-interest are not the driving forces c. The resources are used to achieve certain socio- 	<ul style="list-style-type: none"> a. Government itself must run important and selected industries and eliminate the free play of profit motive and self-interest.

Government Interference	<p>economic objectives.</p> <p>d. Centrally planned economy</p> <p>e. Absence of Consumer Choice-</p> <p>f. Relatively Equal Income Distribution-</p> <p>g. Minimum role of Price Mechanism or Market forces-</p> <p>h. Absence of Competition</p>	
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6. Merits of each type of economy

Capitalist economy	Socialist economy	Mixed Economy
<p>a) Self-regulating through price mechanism.</p> <p>b) Rewards efficiency and punishes inefficiency.</p> <p>c) Faster economic growth</p> <p>d) Optimum allocation of resources</p> <p>e) Operative efficiency.</p> <p>f) Lower cost of production</p> <p>g) Better standard of living of consumers</p> <p>h) Incentive for innovation and Technological progress.</p> <p>i) Right to private Property</p> <p>j) No costs for collecting and processing of information</p>	<p>a) Equitable distribution of wealth and income</p> <p>b) Rapid and balanced economic development</p> <p>c) Planned Economy-</p> <p>d) Minimum Wastage and optimum utilisation of resource-</p> <p>e) Unemployment is minimized,</p> <p>f) Absence of profit motive</p> <p>g) Right to work and minimum standard of living</p> <p>h) High Social security</p>	<p>a) Economic freedom and existence of private property</p> <p>b) Price mechanism</p> <p>c) Consumer sovereignty and freedom of choice.</p> <p>d) Appropriate incentives</p> <p>e) Encourages enterprise and risk taking.</p> <p>f) Advantages of economic planning</p> <p>g) Comparatively greater economic and social equality and freedom</p> <p>h) No cut throat competition</p>

7. Demerits of each type of economy

Capitalist economy	Socialist economy	Mixed Economy
<p>a) Precedence of property rights over human rights.</p> <p>b) Inequality and social injustice</p> <p>c) Wide differences in economic opportunities.</p> <p>d) Does not represent the</p>	<p>a) Inefficiency and delays, corruption, red-tapism, favoritism,</p> <p>b) All material means of production are under the control and direction of state.</p> <p>c) Takes away right of private property.</p>	<p>a) Excessive controls the private sector.</p> <p>b) Poor implementation</p> <p>c) Undue delays</p>

<p>real needs of the society.</p> <p>e) Exploitation of labour</p> <p>f) Consumer sovereignty is a myth</p> <p>g) Misallocation of resources</p> <p>h) Less of merit goods</p> <p>i) Unplanned production.</p> <p>j) Waste of productive resources</p> <p>k) Formation of monopolies</p> <p>l) Environmental degradation.</p>	<p>d) No incentive for hard work</p> <p>e) Administered prices</p> <p>f) State monopolies become uncontrollable</p> <p>g) Consumers have no freedom of choice.</p> <p>h) No importance to personal efficiency and productivity.</p> <p>i) The extreme form of socialism is not at all practicable</p>	
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