

CHANAKYA 2.0[®]

For CA Foundation

One Shot

ECONOMICS

**Nature & Scope of
Business Economics**

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TOPICS

to be covered

- 1 Unit – 1 --- Introduction
- 2 Unit – 2 --- Basic problems of an economy & Role of price mechanism
- 3 ICAI MODULE MCQs and PYQs

What is Business all about?

What is Economics about?

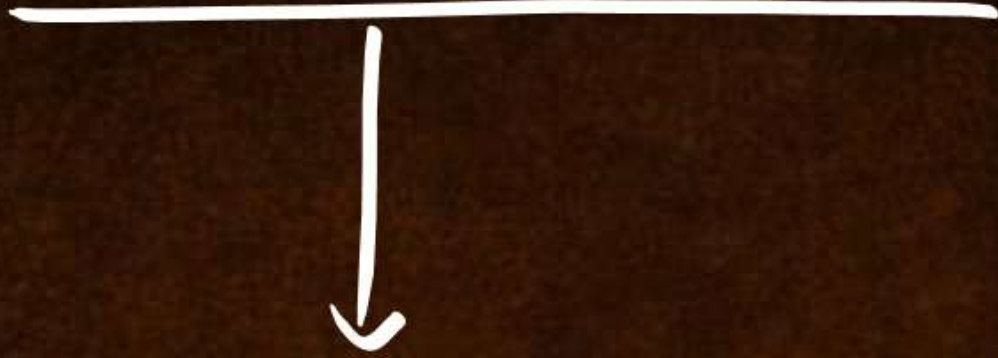


Economic Activity

Poultry, farming,
Banking, Education

What is Business all about?

What is Economics about?



Non-Profit
organisation

→ Surplus

Profit making
organisation

→ Profit ✓



Decision

The term 'Economics' owes its origin to the Greek word 'Oikonomia' which means 'household'.

Till 19th century, Economics was known as 'Political Economy'.

The book named 'An Inquiry into the Nature and Causes of the Wealth of Nations' (1776) usually abbreviated as 'The Wealth of Nations', by Adam Smith is considered as the first modern work of Economics.

↓
father of Economics



Business Economics →
←
Joel Dean



Scarcity → Shortage

$$\begin{array}{rcl} D \rightarrow & 10,000 & \\ S \rightarrow & 1000 & \end{array} \quad \left. \vphantom{\begin{array}{rcl} D \rightarrow & 10,000 & \\ S \rightarrow & 1000 & \end{array}} \right\} \underline{9000}$$



Topic: Economic problem



It is the Problem of making choice. ✓

human
wants

↓
unlimited

5000

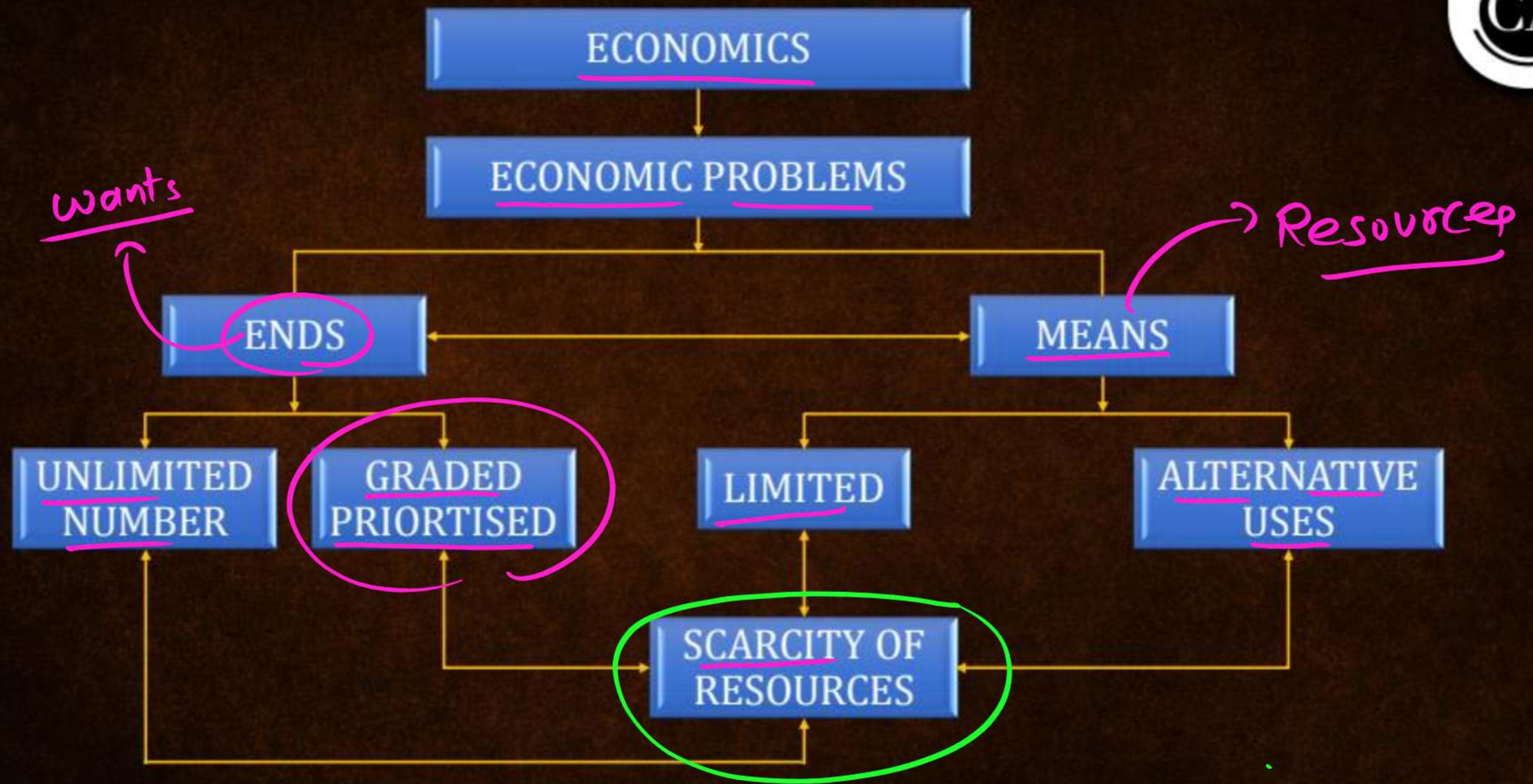
milk

Alternative / many uses

The fundamental facts :

- (i) 'Human beings have unlimited wants'; and
- (ii) 'The means to satisfy these unlimited wants are relatively scarce' form the subject matter of Economics.

→ Resource

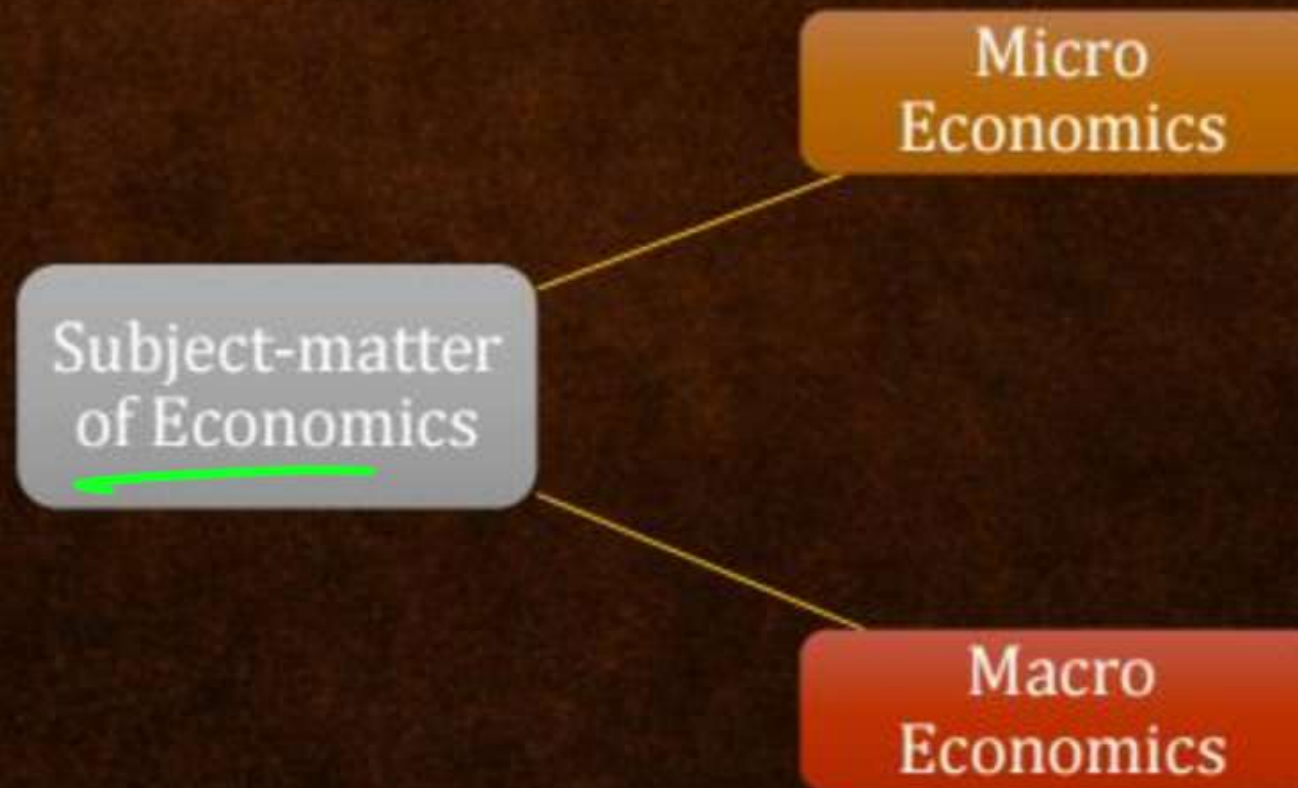




Topic: 2 parts of Economics



Economics has been broadly ^{divided} in- to two major parts i.e. Micro Economics and Macro Economics.



~~MICRO~~

vs

~~MACRO~~

↓
Individual

↓
Aggregate

↓
Totality

Micro Economics is basically the study of the behavior of different individuals and organizations within an economic system. It does not explain what is happening in the wider economic environment.

We mainly study the following in Micro-Economics:

- (i) Product pricing;
- (ii) Consumer behavior;
- (iii) Factor pricing; ✓ → Inputs
- (iv) The economic conditions of a section of people;
- (v) Behavior of firms; and
- (vi) Location of industry.



Macro Economics is the study of the overall economic phenomena or the economy as a whole, rather than its individual parts

A few areas that come under Macro Economics are:

- (i) National Income and National Output;
- (ii) The general price level and interest rates;
- (iii) Balance of trade and balance of payments;
- (iv) External value of currency;
- (v) The overall level of savings and investment; and
- (vi) The level of employment and rate of economic growth.

foreign Exchange rate

↓
GDP ↑



Business

+

Economics

⇓

Business Eco.

| Managerial Eco.

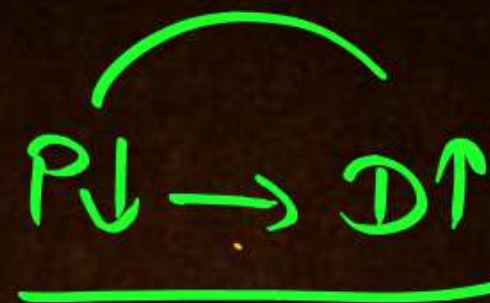
Eco.

↓

Applied Eco.

↓
Business Eco.

The nature of Business Economics:



- 1. Business Economics is a Science:** Science is a systematized body of knowledge which establishes cause and effect relationships. Business Economics integrates the tools of decision sciences such as Mathematics, Statistics and Econometrics with Economic Theory to arrive at appropriate strategies for achieving the goals of the business enterprises. It follows scientific methods and empirically tests the validity of the results.
- 2. Business Economics is an art** as it involves practical application of rules and principles for the attainment of set objectives.

3. **Based on Micro Economics:** Business Economics is based largely on Micro-Economics. Since Business Economics is concerned more with the decision making problems of individual establishments, it relies heavily on the techniques of Micro economics. ✓✓
4. **Incorporates elements of Macro Analysis:** A business unit does not operate in a vacuum(alone) . It is affected by the external environment of the economy in which it operates such as, the general price level, income and employment levels in the economy and government policies with respect to taxation, interest rates, exchange rates, industries, prices, distribution, wages and regulation of monopolies.

✓
5. Use of Theory of Markets and Private Enterprises: Business Economics largely uses the theory of markets and private enterprise. It uses the theory of the firm and resource allocation in the backdrop of a private enterprise economy.

★ 6. Pragmatic in Approach: Micro-Economics is abstract (imaginary) and purely theoretical and analyses economic phenomena under unrealistic assumptions. In contrast, Business Economics is pragmatic in its approach as it tackles practical problems which the firms face in the real world.

7. Interdisciplinary in nature: Business Economics is interdisciplinary in nature as it incorporates tools from other disciplines such as Mathematics, Operations Research, Management Theory, Accounting, marketing, Finance, Statistics and Econometrics.

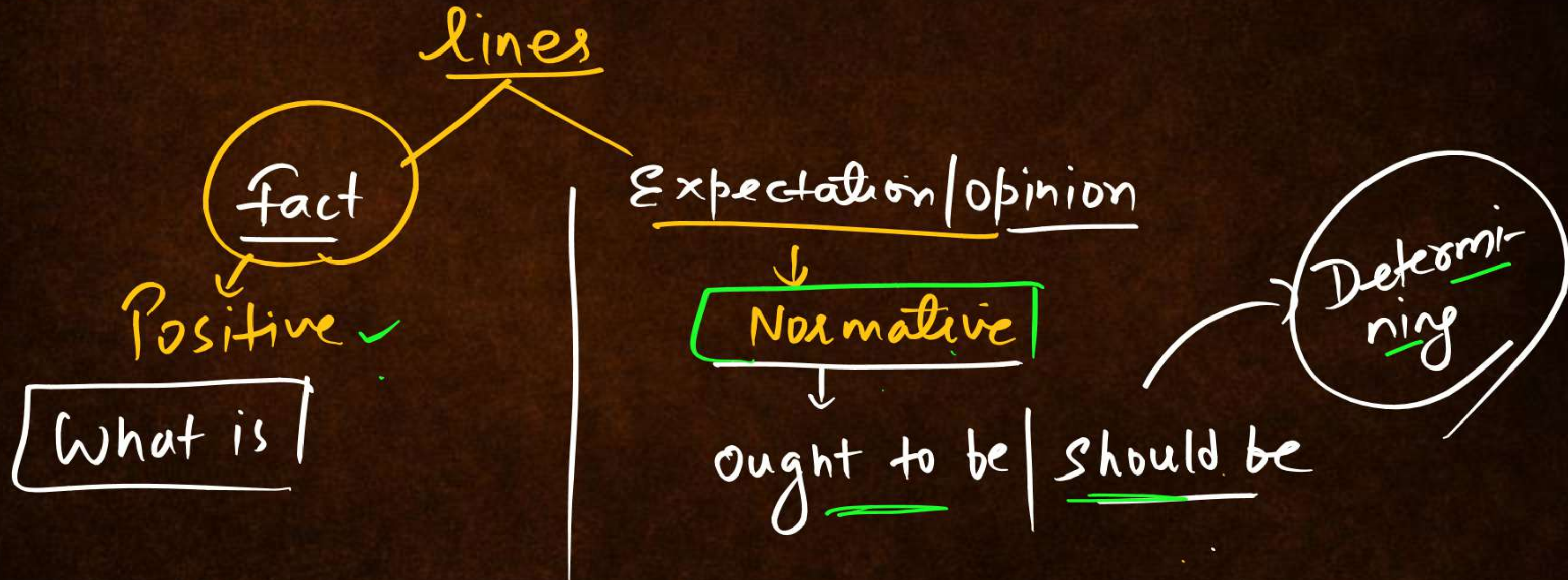
✓
8. Normative in Nature: ✓ Business Economics is generally normative or prescriptive in nature.

Business Economics combines the essentials of normative and positive/descriptive economic theory, the emphasis being more on the former than the latter.

↓
focus



Topic: Normative and Positive Economics



MICRO + MACRO

↓
largely

) Heart of
Business Eco.

Normative + Positive

↓
generally



QUIZ!

#Q. Which of the following statements is/are correct regarding business economics?

- A** Business economics attempts to indicate how business policies are firmly rooted in economic principles
- B** Business economics uses micro economic analysis of the business unit and macro economic analysis of business environment
- C** Business economics takes a pragmatic approach towards facilitating an integration between economic theory and business practices
- D** All the above

D

QUESTION




#Q. Which of the following is a part of microeconomics?

- A** Factor pricing ^{input} **A**
- B** National income
- C** Both (1) and (2) are correct
- D** Both (1) and (2) are incorrect

QUESTION



#Q. The term 'Economics' owes its origin to the Greek Word.

- A** Aikonomia
- B** Wikonornia
- C** Oikonomia 
- D** None of the above

QUESTION



#Q. Adam Smith Published his master Piece "An enquiry into the nature and causes of wealth of Nations" in the year_____.

A

1776

A

B

1786

C

1789

D

1790

QUESTION



#Q. Oikonomia means _____.

- A** Industry
- B** Management of household B
- C** Services
- D** None of these

QUESTION



#Q. Business Economics is also known as? ✓

A Applied Economics

B Managerial Economics **B**

C Micro Economics

D All of the above

QUESTION



#Q. Concept of Business Economics was given by:

- A** Joel Dean A
- B** Alfred Marshall
- C** Adam Smith
- D** L. Robbins

QUESTION



#Q. _____ defined Business Economics in terms of the use of economic analysis in the formulation of business policies.

A

Joel Dean

A

B

Karl Marks

C

Adam Smith

D

Schumpeter

QUESTION



#Q. Micro economics does not study_____.

A Consumer behavior

B Factor Pricing

C General Price Level

D Firms Equilibrium

→ macro

#Q. Micro Economics is the study of :

units

- A** Individual parts of the economy
- B** The economy as a whole
- C** Choice Making
- D** Development of the economy

#Q. Business Economics relies heavily on the techniques of _____.

↓
largely

A

Micro Economics

A

B

Macro Economics

C

Normative Science only

D

Economics Discipline Only

#Q. Which of the following is a normative statement?

↳ Should be

- A** Planned economies allocate re-sources via government departments ✓
- B** Most transitional economies have experienced problems of falling output and rising prices over the past decade
- C** There is a greater degree of consumer sovereignty in market economies than planned economies
- D** Reducing inequality should be a major priority for mixed economies D

#Q. An example of 'positive' economic analysis would be:

- A** ✓ An analysis of the relationship between the price of food & the quantity purchased (A) (D)
- B** Determining how much income each person should be guaranteed
- C** Determining the 'fair' price for food
- D** Deciding how to distribute the output of the economy

QUESTION



#Q. Business Economics is ✓ in its approach as it tackles practical problems which the firm faces in the real world.

- A** Scientific
- B** Pragmmatic
- C** Theoretical
- D** Mathematical

B

QUESTION



#Q. Business Economics is _____.

- A** Abstract and applies the tools of Microeconomics
- B** Involves practical application of economic theory in business decision making
- C** Incorporates tools from multiple disciplines
- D** (B) and (C) above

D

Pragmatic
Inter-discipline

QUESTION



#Q. Business Economics is also known as?

A Applied Economics

B Managerial Economics

C Micro Economics

D All of the above

B

QUESTION



#Q. Economics is the study of:

- A** How society manages its unlimited resources ✓
- B** How to reduce our wants until we are satisfied ✓
- C** How society manages its scarce resources. [C]
- D** How to fully satisfy our unlimited wants



Topic: Scope of Business Economics

ICAI module page no. - 1.11



The scope of Business Economics is quite wide. There are two categories of business issues to which economic theories can be directly applied, namely:

1. Microeconomics applied to operational or internal Issues
2. Macroeconomics applied to environmental or external issues

(1) Microeconomics applied to operational or internal Issues

- a. Demand analysis and forecasting: ✓
- b. Production and Cost Analysis:
- c. Inventory Management:
- d. Market Structure and Pricing Policies:
- e. Resource Allocation:
- f. Theory of Capital and Investment Decisions: ✓
- g. Profit Analysis:



2. Macroeconomics applied to environmental or external issues

- a) the type of economic system ✓
- b) stage of business cycle 
- c) the general trends in national income, employment, prices, saving and investment.
- d) Government's economic policies like industrial policy, competition policy, monetary and fiscal policy, price policy, foreign trade policy and globalization policies
- e) working of financial sector and capital market
- f) socio-economic organizations like trade unions ✓, producer and consumer unions and cooperatives.
- g) social and political environment.



QUIZ!

#Q. Mr. Shaktimaan hired a business consultant to guide him for growth of his business. The consultant visited his factory and suggested some changes with respect to staff appointment, loan availability and so on. Which approach is that consultant using?

A Micro economics

A

B Macro economics

C None of the above

D Both (1) and (2)

#Q. Which of the following statements is correct?

- A** Micro economics is important for study of a particular household and a particular firm ✓
- B** Macro economics is important for study of economic conditions of a country ✓
- C** None of the above
- D** Both (A) and (B) D

QUESTION



#Q. Business Economics involves the elements of _____.

A Micro Environment

B Macro Environment

C Both (A) and (B)



D None of the above



Topic: Difference Between Economics & Business Economics



| Basis of Difference | Economics | Business Economics |
|---------------------|---|---|
| <u>Meaning</u> | It involves the <u>framing</u> of economic principles to solve economic problems. | It involves the <u>application</u> of economic principles to solve economic problems. |
| <u>Character</u> | It is <u>microeconomic</u> as well as <u>macroeconomic</u> in character. | It is <u>microeconomic</u> in character. |
| <u>Main Task</u> | The <u>fulfilment</u> of <u>needs</u> of individuals as well as entities. | <u>Proper decision making</u> in a particular business entity. |
| <u>Nature</u> | It is <u>positive</u> as well as <u>normative</u> in nature. | It is only <u>normative</u> in nature. |
| <u>Scope</u> | It has a <u>wider scope</u> . | It has a <u>comparatively narrow scope</u> . |



| Basis of Difference | Economics | Business Economics |
|--------------------------------|---|--|
| <u>Branches</u> | It has <u>business economics</u> as its applied branch. | It is an <u>applied branch</u> of economics. |
| <u>Concerned with</u> | All the theories from <u>production to consumption</u> including <u>distribution</u> . | It is concerned with only <u>profit theory</u> ignoring other theories. |
| <u>Analysis Involved</u> | It includes the <u>analysis</u> of <u>macro level issues</u> like <u>growth</u> , <u>inflation</u> and <u>employment</u> , etc. | It includes the <u>analysis</u> of <u>micro level issues</u> like <u>demand</u> , <u>supply</u> and <u>profit</u> etc. |
| <u>Concentration</u> | It <u>concentrates only on the economic aspects</u> of any business problem. | It concentrates on <u>both economic as well as non-economic aspects</u> business problem. |
| <u>Validity of Assumptions</u> | It is based on certain assumptions. | Some <u>assumptions</u> become <u>invalid</u> when applied. |



Topic: Central Problems of an Economy

The central economic problem is further divided into four basic economic problems. These are.

- (1) What to Produce? ✓
- (2) How to Produce?
- (3) For whom to produce?
- (4) What provisions (if any) are to be made for economic growth?



Topic: What to Produce?



It refers to the problem of making choice of the good to be produced in an economy.

There are millions of goods to be produced in an economy.

For example:-

- (1) capital goods like machinery, tractor etc.
- (2) consumer goods like toothpaste, sugar etc.
- (3) war time goods like gun, bomb etc.

Once the selection about the goods to be produced is made then next problem arise of How much to be produced ?



How

Topic: What to Produce?



It refers to the problem of choice related to production technology.

There are two types of production technology :-

- (1) labour intensive technology $L > C$
- (2) capital intensive technology $\rightarrow L < C$

Labour intensive technology refers to the production technic where more labour and less capital is used.

Capital intensive technology refers to the production technic where more capital and less labour is used.



Topic: For whom to Produce?



Another important decision which a society has to take is 'for whom' it should produce. A society cannot satisfy each and every want of all the people. Therefore, it has to decide on who should get how much of the total output of goods and services, i.e. How the goods (and services) should be distributed among the members of the society. In other words, it has to decide about the shares of different people in the national cake of goods and services.

For whom?

100 unit

| | | | |
|-------------|------|------|----|
| <u>Poor</u> | (10) | (90) | 50 |
| <u>Rich</u> | (90) | (10) | 50 |



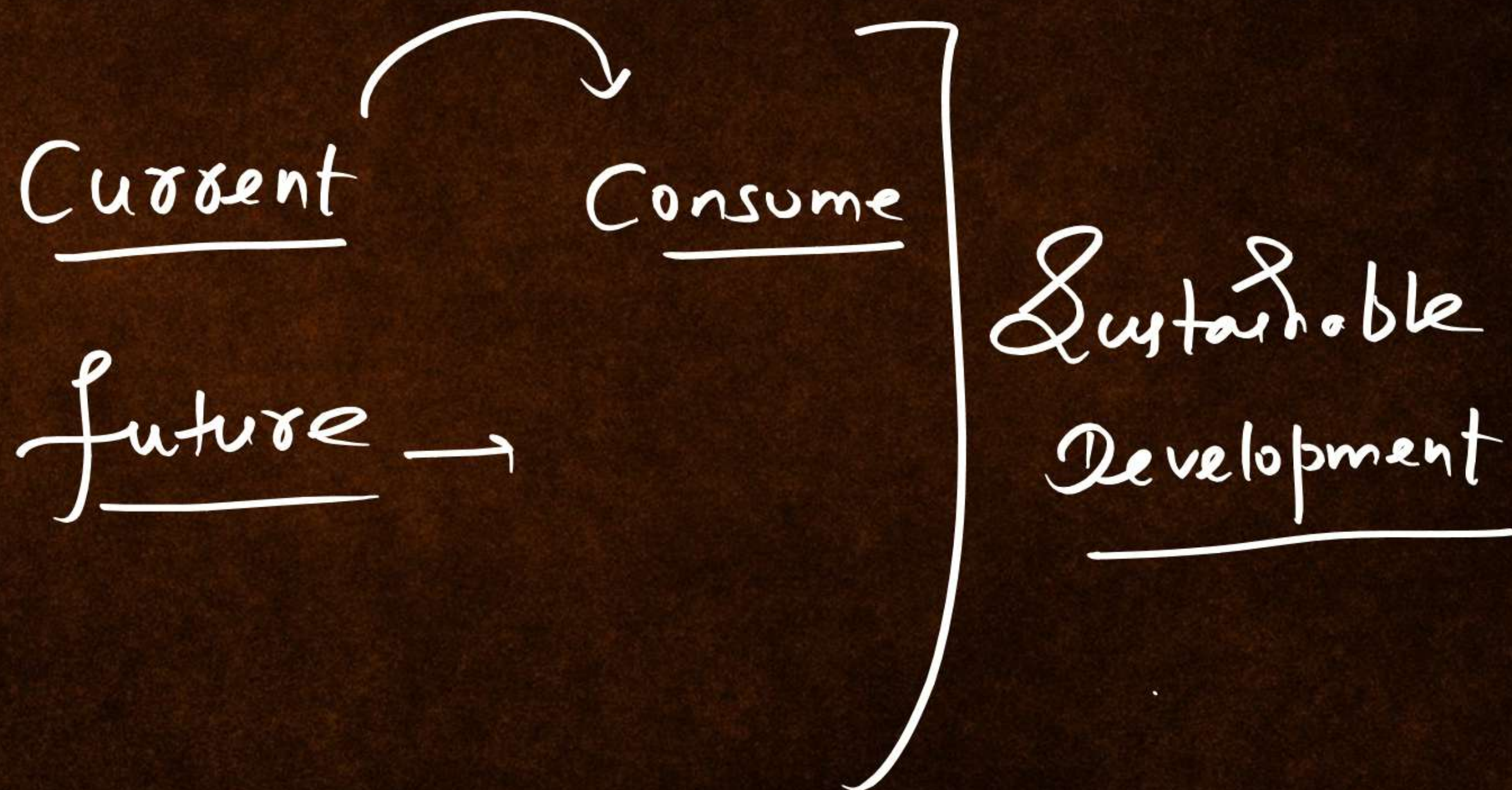
Topic: What Provision Should be Made for Economic Growth?



A society would not like to use all its scarce resources for current consumption only. This is because, if it uses all the resources for current consumption and no provision is made for future production, the society's production capacity would not increase. This implies that incomes or standards of living of the people would remain stagnant, and in future, the levels of living may actually decline. Therefore, a society has to decide.

How much saving and investment (i.e. how much sacrifice of current consumption) should be made for future progress.

slow





QUIZ!

#Q. What implication(s) does resource scarcity have for the satisfaction of wants?

- A** Not all wants can be satisfied. **A**
- B** We will never be faced with the need to make choices
- C** We must develop ways to decrease our individual wants
- D** The discovery of new natural resources is necessary to increase our ability to satisfy wants

QUESTION



#Q. In every economic system, scarcity imposes limitations on _____.


- A** Households, business firms, governments and the nation as a whole
- B** Households and business firms, but not the governments
- C** Local and state governments, but not the federal government
- D** Households and governments, but not business firms

Non-Economic goods



Air

#Q. Economic goods are considered scarce resources because they _____.

- A** Cannot be increased in quantity
- B** Do not exist in adequate quantity to satisfy the requirements of the society 
- C** Are of primary importance in satisfying social requirements
- D** Are limited to man made goods



Topic: Economic Systems & Its Types

Three types of economy:

page no. 1.18

- (1) Capitalist Economy | Free mkt. / Laissez faire
- (2) Socialist Economy | Command / Planned
- (3) Mixed Economy



Topic: Capitalist Economy

Resource

- It is Economic system in which all means of production are owned and controlled by private individuals for profit.
- Private property is the mainstay {backbone} of capitalism and profit motive is its driving force ★
- The government has a limited role in the management of the economic affairs under this system. Some examples of a capitalist economy may include U.S., U.K., Germany, Japan, Mexico, Singapore, etc.



Topic: features of Capitalist Economy

1. Right to private property
2. Freedom of enterprise
3. Freedom of economic choice
4. Profit motive
5. Consumer sovereignty *Supremacy*
6. Competition
7. Absence of govt. interference



Topic: Socialist Economy



The concept of socialist economy was propounded by Karl Marx and Frederic Engels in their work 'The Communist Manifesto' published in 1848.

The erstwhile U.S.S.R. was an example of socialist economy from 1917 to 1990. In today's world there is no country which is purely socialist. Other examples include Vietnam, China and Cuba. North Korea, the world's most totalitarian state, is another example of a socialist economy.



Topic: features of socialistic Economy

- (1) Collective Ownership:
- (2) Economic planning:
- (3) Absence of Consumer Choice
- (4) Relatively Equal Income Distribution
- (5) Minimum role of Price Mechanism or Market forces
- (6) Absence of Competition





Absence of Comptⁿ → Socialistic

Waste of Comptⁿ → Capitalistic



Topic: The Mixed Economy

In a mixed economy, the aim is to develop a system which tries to include the best features of both the controlled economy and the market economy while excluding the demerits of both.

It appreciates the advantages of private enterprise and private property with their emphasis on self-interest and profit motive.



Mixed



Topic: Features of ~~Socialistic~~ Economy

(1) co-existence of private and public sector

In a mixed economy, there are three sectors of industries:

- (a) Private sector: Production and distribution in this sector are managed and controlled by private individuals and groups.
- (b) Public sector: Industries in this sector are not primarily profit-oriented, but are set up by the State for the welfare of the community.
- (c) Combined sector: A sector in which both the government and the private enterprises have equal access, and join hands to produce commodities and services, leading to the establishment of joint sectors.



Topic: Different Economies Comparison

| | <u>Capitalist</u> | <u>Socialist</u> | <u>Mixed</u> |
|---------------------------------------|---|---|--|
| (1) <u>Mainstay</u> | <u>Private property</u> | <u>Socio-economic objective, collective ownership</u> | <u>Best features of both the economies</u> |
| (2) <u>Driving force</u> | <u>Profit motive</u> ★ | <u>Equitable distribution of income</u> ★ | <u>Profit motive as well as relative equitable distribution of income.</u> |
| (3) <u>Interference of government</u> | <u>No interference</u> | <u>Government is the central planning authority</u> | <u>Positive role of government</u> |
| (4) <u>Also known as</u> | <u>Free market economy, Laissez faire economy</u> | <u>Command economy, Centrally planned economy</u> | - |



| | Capitalist | Socialist | Mixed |
|--|---|-----------------------------|---|
| (5) <u>Right to private property</u> | Yes ✓ | <u>Collective ownership</u> | <u>Coexistence of private and public sector</u> |
| (6) <u>Freedom to choice for the consumers</u> | <u>YES</u> | <u>NO</u> | <u>YES</u> |
| (7) <u>Competition (Price mechanism / market forces)</u> ✓ | <u>Prevails</u> ✓ | <u>Does not prevail</u> | <u>Economic fluctuations are avoided</u> |
| (8) <u>Income distribution</u> | <u>Unequal</u> ✓ | <u>Equal</u> | <u>Government tries to bring relatively equal distribution of income</u> |
| (9) <u>Freedom of Enterprise</u> ✓ | <u>Yes, free to produce goods and service</u> | <u>No</u> | <u>Yes, only certain areas may be handled exclusively by government</u> ✓ |



| | Capitalist | Socialist | Mixed |
|--|--|---|---|
| (10) Central Problems of ✓ the economy | | | |
| What to Produce? ✓ | Those goods and services are produced which yields <u>maximum profit</u> | As directed by central government / authority | Those goods that yield maximum profit but even the central authority directs or produces certain essential goods and services ✓ |
| How to produce ✓ | Minimization of cost of production | Nobody shall remain unemployed | Private enterprise focuses on cost minimization whereas government ensures and keeps check on unemployment |
| For whom to produce ✓ | Those who have the buying capacity | For every individual of the economy | For every individual |

Capitalistic → Consumer is king Sovereignty
, consumer Sovereignty
is myth.



QUIZ!

#Q. Consider the following and decide which, if any, economy is without scarcity:

- A** The pre-independent Indian economy, where most people were farmers ✓
- B** A mythical economy where everybody is a billionaire
- C** Any economy where income is distributed equally among its people
- D** None of the above.

D

QUESTION



#Q. Human wants are in response to satisfy their wants?

- A** Unlimited. **A**
- B** Limited
- C** Scarce
- D** Multiple

#Q. Which one of the following is incorrect about Business Economics?

- A** It is applied economics that fills the gap between economic theory & business practice ✓
- B** Business Economics integrates economic theory with business practice ✓
- C** Business Economics is also referred to as Managerial Economics ✓
- D** Business Economics is more concerned with Macro Economics. D

QUESTION



#Q. Administered prices refer to:

- A** Prices determined by forces of demand and supply
- B** Prices determined by sellers in the market
- C** Prices determined by an external authority which is usually the government ✓
- D** None of the above

C

QUESTION



#Q. A mixed economy to solve its central problems relies on-

A Economic planning

B Price mechanism

C Price fixing

D Both (A) and (B).

D

QUESTION



#Q. In a socialist economy, the basic force of economic activity is profit. This statement is- ✓

- A** Correct
- B** Incorrect ✓
- C** Partially correct
- D** None of these

B

#Q. The interference of the government is very limited in-

- A** Socialist economy
- B** Capitalist economy ✓
- C** Mixed economy
- D** All the above

QUESTION



#Q. In a competitive economy, the uncrowned king is-



A Government

B Producer

C Consumer

D Sell



QUESTION



#Q. Wastes of competition are found in-

- A** Capitalist economy ✓ **A**
- B** Socialist economy
- C** Mixed economy
- D** None of these

#Q. Wastes of competition are found in capitalistic economy -

This is because the prices are determined by the free interaction of the forces of demand and supply. It is an automatic self-regulating mechanism which runs with the motive of profit.

QUESTION



#Q. A dual system of pricing exists in-

- A** Capitalist economy
- B** Socialist economy
- C** Mixed economy ✓
- D** None of these



#Q. One of the important features of capitalist economy is-

- A** Economic planning → Socialistic
- B** Price mechanism → Capitalistic (B)
- C** Economic equalities
- D** Social welfare

QUESTION



#Q. The Business Economics incorporates tools from other disciplines such as Mathematics, operations Research, Management theory, Accounting, etc. Therefore, Business Economics is

A Intra-disciplinary

B Inter-disciplinary

C Multi-disciplinary

D Flexi-disciplinary

B

QUESTION



#Q. The operational or internal issues to which economic theories can be directly applied are related with.

- A** Micro Environment ✓ **A**
- B** Macro Environment
- C** Business Economics
- D** Environmental Economics

#Q. Which of the following is not a part of central economic Problem?

- A What to Produce?
- B How to Produce?
- C For whom to Produce?
- D Price fixation of Production

D

QUESTION



#Q. Which one of the following is not an example of capitalist economy?

- A** Japan
 - B** Mexico
 - C** Germany
 - D** Cuba
- D**

QUESTION



#Q. _____ is also called as command economy

- A** Socialist **A**
- B** Capitalist
- C** Mixed economy
- D** None of the above

QUESTION



#Q. Unlimited ends & limited means together present the problem of _____

Handwritten annotations:
An arrow points from the word "ends" to the word "wants".
An arrow points from the word "means" to the word "Resource".

- A** Scarcity of resources
- B** Choice
- C** Distribution
- D** None of the above

Handwritten: B

QUESTION



#Q. Profit motive is a key characteristic of

- A** Socialism
- B** Capitalism **B**
- C** Mixed economy
- D** None of the above



2 Mins Summary

CA

ICAI module

Capitalistic Eco^x

(1) $\overset{\checkmark}{DD}$

(2) SS

(3) $\boxed{\text{Price}} \sim \boxed{C}$

$\boxed{P \times}$



THANK YOU

