

# Nature & Scope of Business Economics

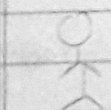
## Unit 1 :- Introduction

### → Introduction :-

• Economics (Scarcy) → Origin from Greek word → 'OIKONOMIA'  
↓ means Household

• Till 19<sup>th</sup> Century, Economics was known as → Political Economics

### • Book



Adam Smith  
[Father of Economics]

→ In 1776 →

Book  
"An inquiry into the Nature and Cause of the Wealth of Nation"

↓ abbreviated as

"The Wealth of Nation"

↓ considered as

First modern work of Economics

• Economics is study of processes by which the relatively scarce resources are allocated to unlimited satisfy unlimited human wants.

### Two Fundamental facts

- (i) 'Human beings have unlimited wants' and
- (ii) 'The means to satisfy these unlimited want are relatively scarce'

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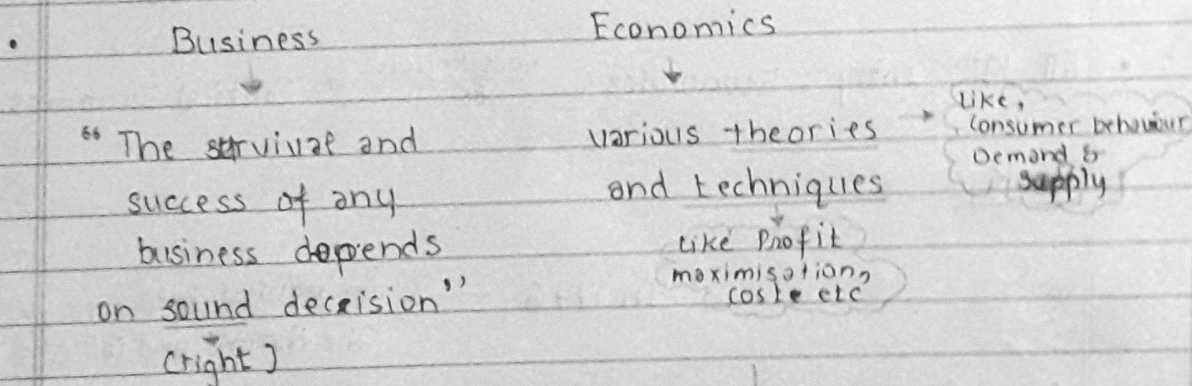
But modern Economists say that it is a narrow definition. small thinking

• In day to day events there are various economic issue [Global Crisis 2008, Corona Pandemic 2019-20]

# Economics theories are hypothetical and simplistic in character.

# Study of Economics cannot ensure that all the problems will be appropriately tackled, but it would enable us to examine a problem in its right perspective.

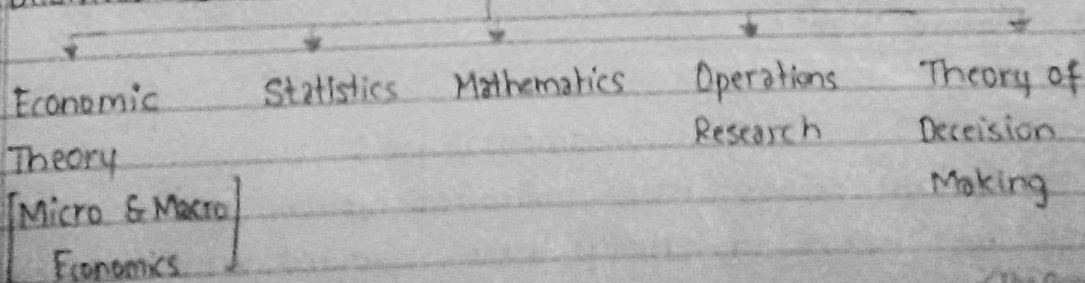
## → Introduction to Business Economics : →



Business Economics integrates Economic theory with Business practice

• Therefore it is known as Managerial Economics or Applied Economics

• Business Economics has close connection with



→ Joel Dean defined Business Economics in the terms of use of use of economic analysis in the formulation of business policies.

→ Nature of Business Economics :- →

(1) Business Economics is a Science :-

- Science → cause-effect relationship. (like - ↑ Price ↓ demand)
- Integrating decision science with economic theory

↓  
Mathematics                  Statistics                  Econometrics

(2) Business Economics is also an Art :-

- Applies practical rules and principal for achieving set objectives.

(3) Based on Micro-economics :-

- Primarily concerned with decision making problems of Individual establishment.

- Business Manager concerned with → (a) achievement of predetermined objectives of business  
(b) ensure long term survival & profitable functioning of organization.

(4) Incorporate elements of Macro analysis :-

- Considered external economic factor impacting business operations

↓  
Price level, income, government policies

↓ like

taxation, interest rate, exchange rate, distribution, wages, and regulations of monopolies.

(5) Use of theory of Markets and Private Enterprises :-

- It uses the theory of the firm and resource allocation in the backdrop of a private enterprise economy.

(6) Pragmatic in Approach :-

(Practical)

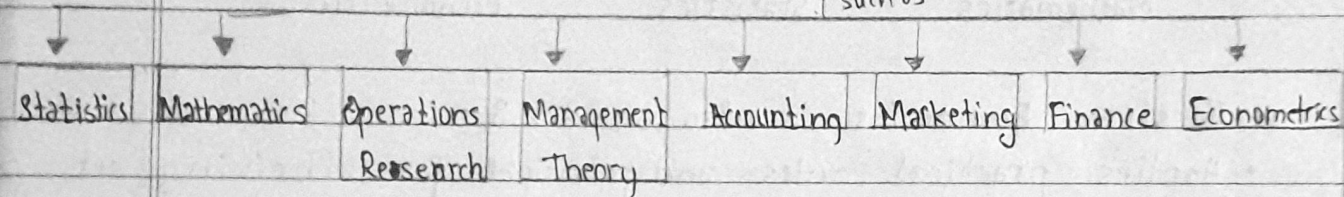
- Addresses real-world practical problems faced by firms.

(7) Interdisciplinary in Nature :-

Different subject

- Integrates tools from various disciplines

such as



(8) Normative in Nature :-

- Economic theory has developed along two lines
  - Positive
  - Normative

Business Economics

based on

**NORMATIVE**

- Nature → Prescriptive
- Include → 'what ought to be'

- Judgement → (1) Does involve value judgement
- (2) Give solution

# Difference between Positive Science and Normative Science

Basis	Positive or Pure Science	Normative Science
1. Developed By	Robbin	Alfred Marshall



• Tools :-

\* Demand & Supply (Individual)

• How to allocate efficiently their scarce resources.

# Example,

\* Product pricing <sup>→ [Output]</sup>

\* Consumer behaviour

\* Factor pricing <sup>→ Input (Raw material, Land, Labour, entrepreneurship)</sup>

\* The economic conditions of a section of people

\* Behaviour of firms

\* Location of Industry

• Tools

Aggregate Demand & Aggregate Supply

• Economy as a whole



total investment, consumption, saving and level of output and employment.

• Example,

\* National income & National Output.

\* General price level & interest rate.

→ Balance of Trade [BOT] & Balance of payment [BOP]

\* External value of currency (Foreign exchange)

\* The overall level of saving & investment.

→ The level of employment and rate of economic growth.

→ scope of Business Economics : →

scope

Internal Issues OR Operational Issues



[this can be solved using MICRO Economics]

External Issues OR Environmental Issues



[this can be solved using MACRO Economics]

(1) Demand analysis and Forecasting  
Studies consumer behaviour and predicts future demand.

The major macro economic factors related to :-

(2) Production & Cost Analysis  
• Production - input-output relationships  
• Cost - Identifies cost behaviour changes with variables like output, time and plant size.

1. The type of economic system: [Capitalist or Socialist]
2. Stage of business cycle.
3. The general trends in national income, employment, prices, saving and investment.

(3) Inventory Management  
• Minimize inventory costs [Work-in-progress, raw material, Finished goods].  
• Use → ABC analysis, simulation & mathematical models.

4. Government's economic policies like industrial policy, competition policy and fiscal policy, foreign trade policy and globalization policies.

(4) Market structure and Pricing Policies :-  
• Analyzes market competition and market power.  
• Determines pricing strategies and product design.  
• Explains price determination under different market conditions.

5. Working of central banks and financial sector and capital market and their regulation.
6. Socio-economic Organisation like trade unions, producer and consumer unions and cooperative.
7. Social and political environment.

(5) Resource Allocation  
• Utilizes tools like linear programming for optimal resource use.

(6) Theory of Capital & Investment

## Decision \*

- Evaluates investment decision for profit maximization.
- Provides criteria for investment project selection and capital efficiency.
- Surplus capital allocation among competing uses.

## (7) Profit Analysis

- Measure and manages profit under ~~an~~ certain condition.
- Useful for future profit planning.

can be predicted

cannot be predicted

## (8) Risk and Uncertainty Analysis

- Helps in efficient decision making and future planning based on past data and predictions.
- Assesses risk and uncertainties.

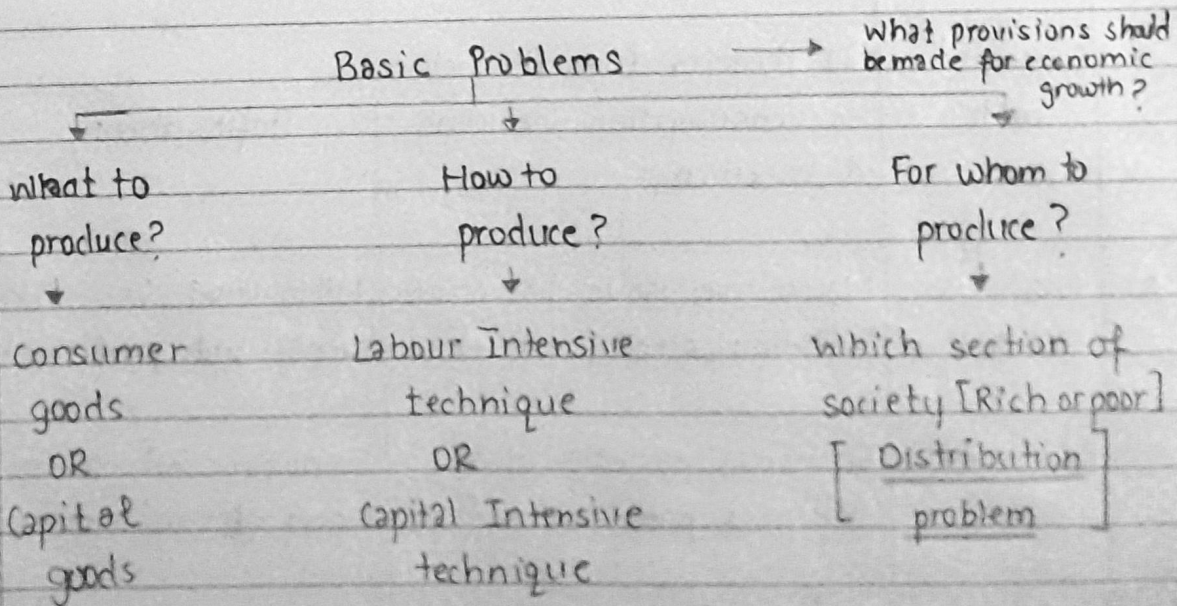
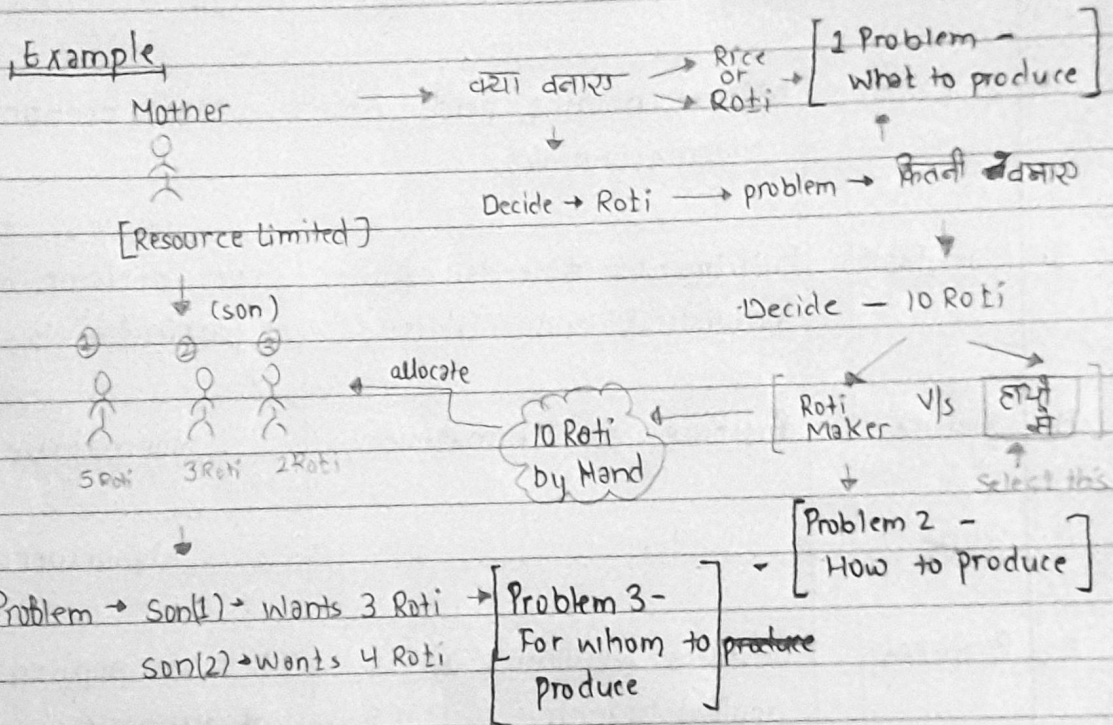


## → Difference between Economics and Business Economics →

Basis	Economics	Business Economics
1. Meaning	It involves the framing of economic principles to solve economic problems.	It involves the application of economic principles to solve economic problems.
2. Character	Microeconomics and Macroeconomics	Macroeconomics
3. Main Task	Fulfilment of needs of individual and entities.	Proper decision making in a particular business entity.
4. Nature	Positive and Normative	Normative
5. Scope	Wider	Narrower
6. Branches	Business economics as its applied branch.	It is an applied branch of economics. (It is a part)
7. Concerned with	All theories from production to consumption including distribution	Profit theory
8. Analysis Involved	Macro level issue like growth, inflation, employment etc	Micro level issue like demand, supply and profit etc
9. Concentration	Economic aspects of any business problems.	Economic and non-economic aspect of any business problems.
10. Validity of Assumptions	Based on certain assumption	Some assumptions become invalid when applied.

# Unit 2 :- Basic Problems of An Economy and Role of Price Mechanism

→ Basic problems of an economy :- →



1. What to produce?

- Limited resource force choices about which goods & services to produce
  - Consumer goods → Bread, egg, car, T.V. etc
  - Capital goods → Machinery, Plants etc.
- Decision involves quantities as well.  
Eg:- how much wheat?  
how many hospitals?

2. How to produce?

- Different production techniques exist and their costs
  - Labour intensive techniques → handlooms etc
  - Capital intensive techniques → power looms for cloth
- Goal 3 - Use resources efficiently

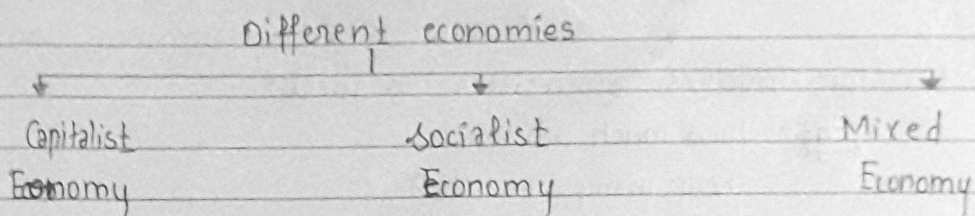
3. For whom to produce?

- Unlimited wants exceeds production, so distribution is crucial.
- Decisions involves who gets what share of the total output (National cake).  
refers to the total output of goods and services produced in a country.

4. What provision should be made for economic growth?

- Balancing current consumption with future need is essential.
- Saving & investment [sacrificing current consumption] are needed for future production/progress and higher living standards. [like sustainable development]

# Economic System, refers to the sum total of arrangements for the production and distribution of goods and services in a society.



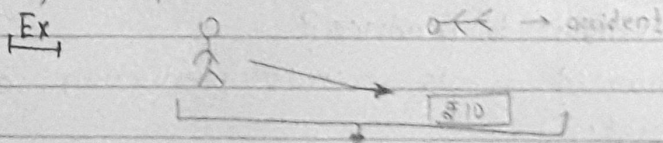
→ Capitalist Economy : →

[Free Market Economy OR laissez-faire]

Policy of leaving things to take their own course

Eg :- US Economy, South Korea, Hong Kong etc.

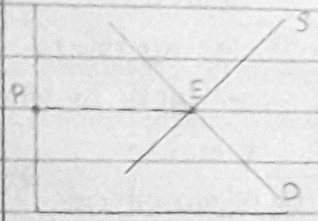
→ Private Property & Profit Motive



Means - Capitalist economy is selfish nature

Features	Merits	Demerits
1. Right to private property	1. Self-regulatory price mechanism	1. <u>Inequality and social injustice</u>
2. Freedom of enterprise	2. Greater efficiency and incentive to work.	Two classes of society
3. Freedom of economic choice.	3. Economic growth is faster	<div style="display: flex; justify-content: space-around;"> <div>haves [Rich]</div> <div>have-nots [Poor]</div> </div>
4. Profit Motive	4. Optimum utilisation of resources	2. Property rights greater than human rights
5. Consumer Sovereignty <small>Supremacy power</small>		
6. Competition [high]		

- |   |   |  |
|---|---|--|
| 7. Absence of government's interference                           | 5. Consumer are benefited [Divided in real price]         | 3. Demand pattern does not represent real needs of society like Alcohol etc. |
| 8. Prices are determined by the market forces of demand & supply. | 6. Freedom of choice                                      | 4. No security of employment   |
|   | 7. It rewards men of initiative and punishes inefficient. | 5. Consumer Sovereignty is myth. [Consumer exploitation]                     |
|   | 8. Democratic framework is there.                         | 6. less of merits goods (like education or health care)                      |
|   |   | 7. Economic instability and Formulation of Monopolies                        |
|   |   | 8. Misallocation of resources  |



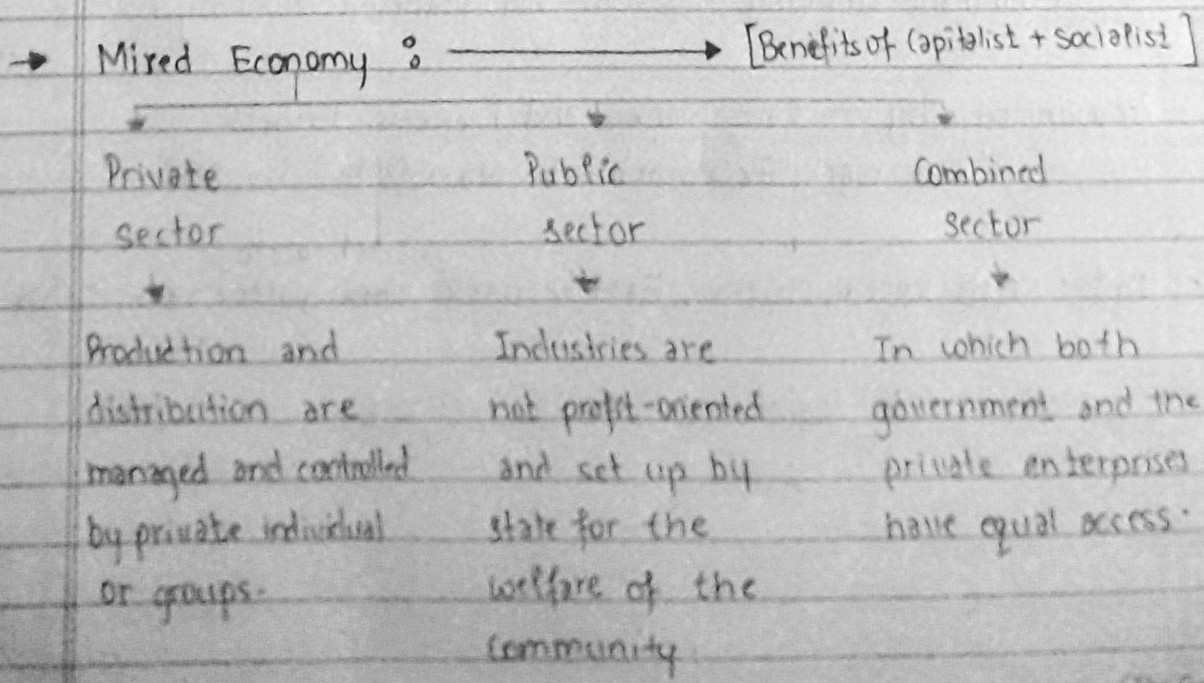
→ Socialist Economy % →

[Command Economy or Centrally planned Economy]

- Propounded by - Karl Marx and Frederic Engels  
Book or work "The Communist Manifesto" in 1848.
- Eg:- North Korea, China, Earlier USSR <sup>[1917 to 1990]</sup> etc., Vietnam, Cuba etc.

Motive → social and public welfare

Features	Merits	Demerits
1. Collective ownership	1. Equitable distribution of wealth and income	1. Inefficiency, Red Tapisim, <sup>paying price to govt. to produce</sup> favouritism etc.
2. Economic planning	2. Balance & Rapid economic development.	2. less freedom of choice.
3. No consumer choice.	3. No wastage of resources on advertisement.	3. No incentives for hardwork in form of profit.
4. Relatively equal Income distribution	4. less employment and Business fluctuation.	4. Administered prices [every product price determined by govt.]
5. Minimum Role of Price Mechanism (Demand & Supply) -	5. Ensure right to work and freedom from hunger or minimum standard of living to all people.	5. State monopolies
6. Absence of Competition	6. Labourers and consumer as protected from exploitation.	
7. social welfare motive.	7. It is a planned economy.	



→ Solutions to central problems in capitalist economy :- →

What to produce?	How to produce?	For whom to produce?
<ul style="list-style-type: none"> <li>• Entrepreneurs aim for maximum profits</li> <li>• <u>Consumer Preference</u> :- Drive production choice.</li> </ul>	<ul style="list-style-type: none"> <li>• Entrepreneurs choose <u>cost-minimizing techniques</u>.</li> <li>• <u>Relative factor Prices</u> :-</li> </ul>	<ul style="list-style-type: none"> <li>• Goods produced for those with <u>buying capacity</u>.</li> <li>• <u>Income determination</u> :-</li> </ul>
<p><u>Ex</u> :-</p> <p>(1) Higher demand for cars → higher prices → increased production</p> <p>(2) Lower demand for cloth → lower prices → decreased production</p>	<p>(1) Cheap labour → labour intensive methods</p> <p>(2) Expensive labour / Machinery → capital intensive methods.</p>	<p>(i) Work amount</p> <p>(ii) Factor prices</p> <p>(iii) Property ownership</p> <ul style="list-style-type: none"> <li>• Higher income → higher buying capacity → higher demand for goods.</li> </ul>

→ Deciding about Consumption, Saving and Investment :- →

(i) Consumer :-

Consumption and saving are done by consumer.

(ii) Entrepreneurs :-

• Investment are done by entrepreneurs.

• Investments are driven by rate of return on capital.

(iii) Price Mechanism :-

Method distribution, economic growth decision and governs production

(iv) Higher the level of income and interest rate, higher will be the saving.

(v) Market Mechanism :-

(a) Interest rates & return on capital <sup>are nothing</sup> influence but prices of capital on saving.

→ Solutions to central problems in socialist economy :-

What to produce?	How to produce?	For whom to produce?
<ul style="list-style-type: none"> <li>• <u>Central Planning</u> :- government determines what goods &amp; services are needed based on societal needs -</li> </ul>	<ul style="list-style-type: none"> <li>• <u>Central Authority Decision</u> :- Govt. decides production methods</li> </ul>	<ul style="list-style-type: none"> <li>• <u>Equitable Distribution</u> :- Goods &amp; services distributed based on need, not buying capacity.</li> </ul>
<ul style="list-style-type: none"> <li>• <u>Economic Plans</u> :- Like - five - year plans targets - production &amp; resources allocation</li> </ul>	<ul style="list-style-type: none"> <li>• <u>Technology and labour</u> :- Decisions based on achieving social goals rather than minimizing cost.</li> </ul>	<ul style="list-style-type: none"> <li>• <u>State Provision</u> :- Essential services [eg:- healthcare, education] provided free or at subsidized rates.</li> </ul>
<ul style="list-style-type: none"> <li>• <u>Resources Allocation</u> :- Prioritizes essential goods and services [eg:- health-care, education etc].</li> </ul>	<ul style="list-style-type: none"> <li>• <u>Efficiency Goal</u> :- Aim to use resources efficiently to maximize societal benefits.</li> </ul>	<ul style="list-style-type: none"> <li>• <u>Income redistribution</u> :- Policies to <sup>reduce</sup> income inequality [eg:- progressive taxation, welfare programs]</li> </ul>

→ Deciding about Consumption, Saving & Investment :-

- (i) Government Decision :- Central authority directs saving and investment to align with economic plans.
- (ii) Public sector Focus :- Investment primarily in public sector projects and infrastructure.
- (iii) Consumption Management :- Govt controls - availability and distribution of consumer goods.