



Subject: BEM

Chapter:

Category: Assignment 2

1. Mr. Raju runs a hardware store. In the last year his accountant calculated Mr. Raju's profit by comparing his revenue with his expenditure on staff wages, depreciation, loan interest, rent and cost of items sold. The resulting figure was INR 9,50,000 which his accountant calls as profit. His accountant is amazed how Mr. Raju is running such a profitable business

However, Mr. Raju sees things differently:

- He feels he could have earned a salary of INR 8,00,000 had he been working as a software engineer.
- The INR 7,50,000 of the money that he has put in the business, he could have earned INR 48,000 in interest had he left that money in his bank account.

i) Please state which costs are implicit and which are explicit.

ii) Please calculate Mr. Raju normal profit.

iii) Mr. Raju has hired you an Actuary to redo the numbers. Determine the economic profit that he made last year.

iv) Assuming Mr. Raju can sell the bookshop business next year for INR 800,000. What your answer suggests Mr Raju should do next year?

The next year Mr. Raju's accountant again calculate the accounting profits as being INR 8,75,000.

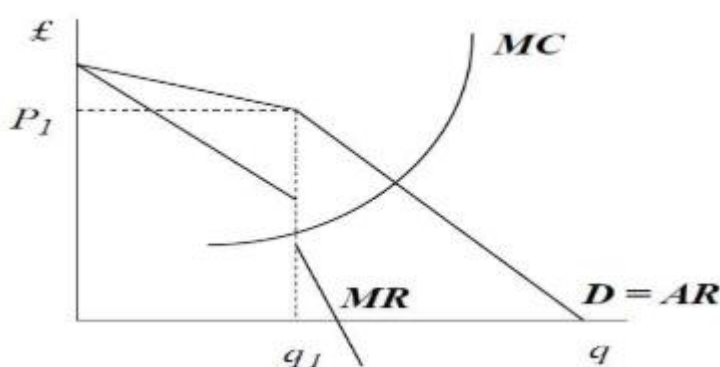
v) Assuming that Mr. Raju's salary as a software engineer would have been INR 8,77,000 and his initial investment in the business would have earned INR 50,000 how will Mr. Raju view this?

2. Describe three ways in which firms can use their market power to the detriment of the consumers. Define each one of them with an example.

3. Suggest ways in which Governments could regulate monopolies and oligopolies.

4. Define economies of scale and describe six main sources of plant economies of scale.

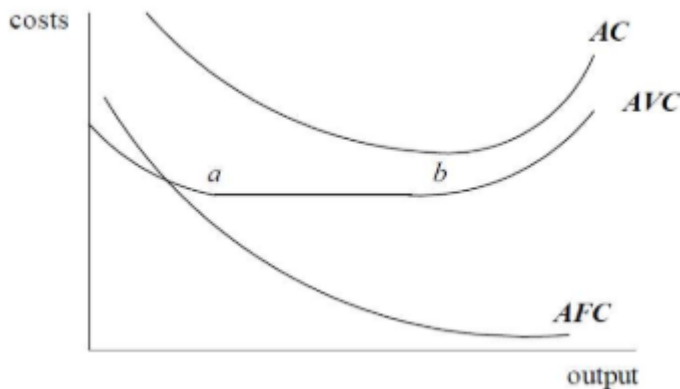
5.



i) State the name of the market structure to which the above demand model applies.

ii) With the help of diagram, explain how the price stability is achieved in this market structure stating the relevant assumptions.

6.



The above diagram shows short run average cost curves of a firm which uses cost based pricing.

i) Explain with the help of given diagram how the firm decides price under cost based pricing.

ii) List the factors that affect the mark up used under cost based pricing.

7. i) Why third party motor insurance is considered as a merit good?

ii) How does advertising affect monopolistic competition?

8. i) Outline the conditions that must hold a firm to be able to practise third- degree price discrimination.

ii) Discuss with the help of examples whether or not price discrimination is in public interest.

9. Consider the following Companies A to E where each is an individual firm operating under a specific market structure.

<i>Company</i>	<i>Marginal cost</i>	<i>Average cost</i>	<i>Average revenue</i>	<i>Marginal revenue</i>
A	10	10	10	10
B	12	9	12	12
C	15	18	20	15
D	9	14	20	14
E	25	20	20	10

- State which company has a short run equilibrium output that may be that of a profit maximising monopolist.
- Give ALL the companies that are making excess profits
- Give ALL the companies that could expand their output and increase their profits
- Give ALL the companies that could be operating in a perfectly competitive environment

10. i. Explain the difference between the law of diminishing returns and the law of diminishing marginal utility.
- ii. Draw a marginal product curve for Good X that you would expect from the laws of diminishing returns (assume initially there is some increasing returns). Clearly indicate on the curve a region of negative marginal product and label your axes carefully.
- iii. Draw a marginal utility curve for Good X that you would expect from the law of diminishing marginal utility. Indicate on the curve a region of negative marginal utility and label your axes carefully.



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