SYLLABUS - BUSINESS ECONOMICS


Unit II: Theory of Utility - Theory of utility, cardinal and ordinal utility theory, law of diminishing marginal utility, law of Equimarginal utility, indifference curves, consumer equilibrium, consumer surplus.

Unit III: Concept of Demand and Supply - Different concepts of demand, demand curve, Determinants of demand, Law of demand, Demand forecasting methods, Market equilibrium, Concepts of elasticity. Concept of supply, supply curve, Conditions of supply, Elasticity of supply, Economies of scale and scope.

Unit IV: Production and Cost Analysis - The production function, Short-run and Long-run production function, law of diminishing returns and returns to scale. Fixed, variable and other cost concepts, least cost-input combination, Relationship between production and cost.

<table>
<thead>
<tr>
<th>S.no</th>
<th>Contents</th>
</tr>
</thead>
<tbody>
<tr>
<td>1</td>
<td>Basic concepts</td>
</tr>
<tr>
<td>2</td>
<td>Business Economics</td>
</tr>
<tr>
<td>3</td>
<td>Features of Business Economics</td>
</tr>
<tr>
<td>4</td>
<td>Objectives of Business Economics</td>
</tr>
<tr>
<td>5</td>
<td>Scope of Business Economics</td>
</tr>
<tr>
<td>6</td>
<td>Micro and Macro Economics</td>
</tr>
<tr>
<td>7</td>
<td>Basic problems of an economy</td>
</tr>
<tr>
<td>8</td>
<td>Basic / fundamental concepts of Business Economics</td>
</tr>
<tr>
<td>9</td>
<td>Optimization</td>
</tr>
<tr>
<td>10</td>
<td>Economics of information</td>
</tr>
<tr>
<td>11</td>
<td>Macro economics and micro economics of information</td>
</tr>
<tr>
<td>12</td>
<td>Role of Business Economist</td>
</tr>
<tr>
<td>13</td>
<td>Responsibility of Business Economist</td>
</tr>
<tr>
<td>14</td>
<td>Business economics and other disciplines</td>
</tr>
<tr>
<td>15</td>
<td>Importance / significance of Business Economics</td>
</tr>
</tbody>
</table>

If you have any doubts/queries, you can contact me on 8185895470; 9533571700 or “m.sivaram100@gmial.com”
BASIC CONCEPTS OF ECONOMICS

1. Wants:
   "Want" is defined as having a strong desire for something. The word "need" is defined as lack of the means of subsistence. In every arena of life, the two concepts are opposing elements. The basic needs of man include food, clothing and shelter. Human needs are many. They are both tangible and intangible. Tangibles include things that we can touch and feel like need for a vehicle or cell phone. Intangibles are only felt like satisfaction, happiness, jealousy etc. Wants are unlimited. As soon as one ant is satisfied another arises and this process goes on.

2. Scarcity:
   When we talk of scarcity within an economic context, it refers to limited resources. These resources are the inputs of production: land, labor and capital which are used for satisfying human wants. The basic economic problem that arises because of this limited resources is that people have unlimited wants but resources are limited. This creates scarcity. For example: A student wants to purchase a book worth Rs. 100, but he has got only Rs. 50. This creates scarcity of money. In the same way we face so many situations in which we have numerous wants but the resources are limited. Thus, we make our own preferences according to scarcity and sacrifice less pressing wants for those which are preferred. For instance you have two wants. One is to go for a movie and the other is to have food in restaurant. You have limited money. Here, you prefer the more
important one to the less important one. So, movie may be preferred to restaurant. Here, the concept of choice comes into picture which finally leads to opportunity cost.

3. **Scale of Preference:**

   It is defined as a list of unsatisfied wants arranged in the order of their relative importance. In other words, it is the list showing the order in which we want to satisfy our wants according to priority. In scale of preference, the most important wants come first and the less important wants come next. Choice therefore arises because human wants are unlimited but the resources are limited and scarce.

4. **Choice:**

   It can be defined as a system of selecting or choosing one out of a number of alternatives.

   Choice arises as a result of scarcity of resources. Since it is extremely difficult to produce all that we need choice has to be made by accepting or taking up the most pressing wants for satisfaction based on the available resources.

5. **Opportunity Cost:**

   Every scarce goods or activity has an opportunity cost. Opportunity cost of anything is the cost of the next best alternative which is given up. It refers to the cost of foregoing or giving up an opportunity. It is the earnings that would be realized if the available resources were put to some other use. It implies the income or benefit foregone because a certain course of action has been taken. Thus opportunity costs are measured by the sacrifices made in
the decision. If there is no sacrifice involved by a decision there will be no opportunity cost. It is also called alternative cost or transfer cost. The opportunity cost of using a machine to produce one product is the income forgone which would have been earned from the production of other products. If the machine has only one use, it has no opportunity cost. Similarly, the opportunity costs of funds invested in one's own business is the amount of interest earned if the amount had been used in other projects.

**BUSINESS ECONOMICS**

Business Economics consists of that part of economic theory which helps the business manager to take rational decisions. Economic theories help to analyze the practical problems faced by a business firm. *Business Economics integrates economic theory with business practice*. It is a special branch of economics that bridges the gap between abstract theory and business practice. It deals with the use of economic concepts and principles for decision making in a business unit. It is also called Managerial Economics or Economics of the Firm. Managerial Economics is economics applied in business decision-making. Hence it is also called *Applied Economics*.

**DEFINITION OF BUSINESS ECONOMICS**

In simple words, business economics is the discipline which helps a business manager in decision making for achieving the desired results. In other words, it deals with the application of economic theory to business management.
According to Spencer and Siegelman, Business economics is "the integration of economic theory with business practice for the purpose of facilitating decision-making and forward planning by management".

According to Mc Nair and Meriam, "Business economics deals with the use of economic modes of thought to analyze business situation".

From the above said definitions, we can say that business economics makes in depth study of the following:

i) Understanding the business in a better way
ii) Identification of the business areas where economic analysis can be applied
iii) Planning for the future based on the past events
iv) Decision making

FEATURES/CHARACTERISTICS OF BUSINESS ECONOMICS

The following characteristics of business economics will indicate its nature:

1. Micro economics:
   Business economics is micro economic in character. This is so because it studies the problems of an individual business unit. It does not study the problems of the entire economy.

2. Normative science:
   Business economics is a normative science. It is concerned with what management should do under particular circumstances. It determines the
goals of the enterprise. Then it develops the ways to achieve these goals. It always tries to match the future with the present.

3. **Pragmatic:**

Business economics is pragmatic (practical). It concentrates on making economic theory more application oriented. It tries to solve the managerial problems in their day-to-day functioning of the business by applying economic concepts and models.

4. **Prescriptive:**

Business economics is prescriptive rather than descriptive. It prescribes solutions to various business problems. Instead of focusing on what had happened, it focuses on what should happen in the future. This particular feature helps the business unit to rectify its own mistakes.

5. **Uses macroeconomics:**

Business economics is also useful to business economics. Macro-Economics provides an intelligent understanding of the environment in which the business operates. Business economics takes the help of macro-economics to understand the external conditions such as business cycle, national income, and economic policies of Government etc.

6. **Uses theory of firm:**

Theory of firm tries to solve business problems to maximize profits. Business economics largely uses the body of economic concepts and principles towards solving the business problems. Business economics is a special branch of economics to bridge the gap between economic theory and managerial practice.

7. **Management oriented:**
The main aim of Business economics is to help the management in taking correct decisions and preparing plans and policies for future. Business economics analyses the problems and give solutions just as doctor tries to give relief to the patient.

8. **Multi disciplinary:**
   Business economics makes use of most modern tools of Mathematics, Statistics and Operations Research in planning, decision etc.

9. **Art and science.**
   Business economics is both a science and an art. As a science, it establishes relationship between cause and effect by collecting, classifying and analyzing the facts on the basis of certain principles. It points out to the objectives and also shows the way to attain the said objectives. On the other hand business economists attain perfection by continuously applying and learning the concepts of business economics. It mostly deals with experience.

**OBJECTIVES OF BUSINESS ECONOMICS**

Business economics provides such tools necessary for business decisions. Business economics answers the five fundamental problems of decision making. These problems are:

(a) What should be the product mix?

(b) Which is the least cost production technique and input mix?

(c) What should be the level of output and price of the product?
(d) How to take investment decisions
(e) How much should be the selling cost.

In order to solve the problems of decision-making, data are to be collected and analyzed in the light of business objectives. Business economics supplies such data to the business economist.

As pointed out by Joel Dean "The purpose of Business economics is to show how economic analysis can be used in formulating business policies".

The basic objective of Business economics is to analyze economic problems of business and suggest solutions and help the managers in decision-making.

The objectives of business economics are outlined as below:

1. To integrate economic theory with business practice.
2. To apply economic concepts: and principles to solve business problems.
3. To employ the most modern instruments and tools to solve business problems.
4. To allocate the scarce resources in the optimal manner.
5. To make overall development of a firm.
6. To help achieve other objectives of a firm like attaining industry leadership, expansion of the market share etc.
7. To minimize risk and uncertainty
8. To help in demand and sales forecasting.
9. To help in operation of firm by helping in planning, organizing, controlling etc.
10. To help in formulating business policies.

11. To help in profit maximization.

Business economics is useful because:

(i) It provides tools and techniques for managerial decisions,
(ii) It gives answers to the basic problems of business management,
(iii) It supplies data for analysis and forecasting,
(iv) It provides tools for demand forecasting and profit planning,
(v) It guides the business economist.

Thus, Business economics offers a number of benefits to organizations. It is also useful to individuals, society and government.

SCOPE (NATURE) OF BUSINESS ECONOMICS

Business economics is a developing science. Its scope is gradually increasing in the modernized world. It covers the following areas

1. **Demand analysis and forecasting:**
   The foremost aspect regarding scope is demand analysis and forecasting. A business firm is an economic unit which transforms productive resources into saleable goods. Since all output is meant to be sold, accurate estimates of demand help a firm in minimizing its costs of production and storage. A firm must decide its total output before preparing its production schedule and deciding on the resources (land, labour, capital and technology) to be employed. Demand forecasts serves as a guide to the management for
maintaining its market share in competition with its rivals, thereby securing its profit.

2. **Cost and production analysis:**

   A firm's profitability depends much on its costs of production. A wise manager would prepare cost estimates for a range of output and identify the factors that cause deviations in cost (increase or decrease). Once the factors are known, it can be possible to determine the optimum level of output where the cost of production would be minimum.

   Production processes are under the charge of engineers but the business manager works to carry out the production function analysis in order to avoid wastage of materials and time. Sound pricing policies (determining selling price) depend much on cost control. The main topics discussed under cost and production analysis are: Cost concepts, cost-output relationships, Economies and Diseconomies of scale and cost control.

3. **Pricing decisions, policies and practices:**

   Another task before a business economist is the pricing of a product. Since a firm's income and profit depend mainly on the price of the product, the pricing policies and all such decisions are to be taken after careful analysis of the nature of the market in which the firm operates. The important topics covered in this field of study are: Market Structure Analysis, Pricing Practices and Price Forecasting.

4. **Profit analysis:**
Each and every business tends to earn profit. It is the profit that increases the competitive strength of a firm in the long run. Economists tells us that profits are the reward for taking risk in uncertain situations. A successful business economist is one who can form more or less correct estimates of costs and revenues at different levels of output. The more successful an economist is in reducing uncertainty, the higher are the profits earned by the business. Therefore, profit-planning and profit measurement constitute the most challenging area of business economics.

5. **Capital management:**
   Another challenging problem for a modern business economist is planning the capital investment. Investments are made in the plant and machinery and buildings which are very high. Therefore, capital management requires top-level decisions. It deals with Cost of capital, Rate of Return and Selection of projects etc.

6. **Effective utilization of business resources:**
   It also studies how well resources can be put to best possible use. Various tools and techniques are used to determine least cost-maximum profit combinations. Methods such as linear programming, networking analysis are used in determining the optimal levels of performance.

7. **Effective use of economic policies for business development:**
   Business economics is micro in character but it is always influenced by macro factors. For example, an individual firm’s idea (micro economic) of manufacturing plastic bags may be affected by the ban on plastic by the government (macroeconomic). Thus economic policies (macro) have to be carefully studied in order to make proper business decisions.
Sometimes economic policies of government also create favourable environment for business units. For instance, Make In India initiative has motivated banks to give more loans to fund seeking companies.

8. **Others**:
   a. Supply analysis
   b. Competitor analysis
   c. Distribution and transportation management
   d. Inventory management:
   e. Linear programming:
   f. Environmental issues:
   g. Business cycles:

**MICRO AND MACRO ECONOMICS**

- Microeconomics is the study of particular markets, and segments of the economy. It looks at issues such as consumer behavior, individual labor markets, and the theory of firms.
- Macro economics is the study of the whole economy. It looks at ‘aggregate’ variables, such as aggregate demand, national output and inflation.

*Micro economics is concerned with:*

- Supply and demand in individual markets
- Individual consumer behavior. e.g. Consumer choice theory
- Individual labor markets – e.g. demand for labor, wage determination
- Externalities arising from production and consumption.
Macro economics is concerned with

- Monetary / fiscal policy. E.g. what effect does interest rates have on whole economy?
- Reasons for inflation, and unemployment
- Economic Growth
- International trade and globalization
- Reasons for differences in living standards and economic growth between countries.
- Government borrowing

Similarities between Microeconomics and Macroeconomics

Although it is convenient to split up economics into two branches – microeconomics and macroeconomics, it is to some extent an artificial divide.

1. Micro principles used in macro economics. If you study impact of devaluation, you are likely to use same economic principles, such as the elasticity of demand to changes in price.

2. Micro effects macro economics and vice versa. If we see a rise in oil prices, this will have a significant impact on cost-push inflation. If technology reduces costs, this enables faster economic growth.
BASIC PROBLEMS OF N ECONOMICS

- **Problem of allocation of resources**

It deals with how scarce resources (‘factors of production’) are distributed among producers, and how scarce goods and services are apportioned among consumers. This analysis takes into consideration the accounting cost, economic cost, opportunity cost, and other costs of resources and goods and services. Allocation of resources is a central theme in economics (which is essentially a study of how resources are allocated) and is associated with economic efficiency and maximization of utility. The problem of allocation of resources arises due to the scarcity of resources.

- **What to produce?**

As resources are scarce, production of all goods and services needed by a society are beyond its capacity. It is simply not possible for any economy to develop according to its plan. So, it has to select a set among various alternatives and meet its requirements in the order of preference. The first priority goes to the basic needs. However, production is guided by profit and profit knows no social justice. An economy should follow social efficiency while allocating resources. The social norms and values should guide to maximize social satisfaction. The problem of what to produce and how much to produce depend on the necessity of the citizens of the country.

- **How much to produce?**
The second question is concerned with the method of production. In some cases, labor may play a major role. It is called labor intensive technology. In others, capital may play a major role. It is called capital intensive. Labor intensive methods create more jobs favoring more employment. It helps in mitigating unemployment problem. Capital intensive production goes for large volume of production. It commends rapid growth rate and the right decision on the current state of the economy.

- **For whom to produce?**

  Production for masses and production for profits are two major choices that every economy has to decide. Basic needs of common people cannot be ignored. Of course, the priority goes to mass production i.e., producing for all. In this quality is determined by the level of living standard, which is the outcome of the development level of the economy. This issue is also related with maintaining social justice. Meeting the basic requirements of all segments of population is the main criteria of resources allocation.

- **Problem of Efficiency in Economy**

  How to run an economy efficiently is the first concern of resource allocation. Economic efficiency is measured in additional welfare achieved without worsening any result. It means that new reallocation of resource must not only be able to maintain the existing level but also achieve new heights. Alternatively, reallocation may be profitable somewhere but incurs losses elsewhere. The main objective is to increase aggregate profitability of the economy.
• **Balance in Economy**

Another purpose of resource allocation is the maintenance of balance among different sectors of an economy. The balance between rural and urban sectors, between home consumption and export promotion, between consumer goods and capital goods and regional balance are the healthy signs of an economy. Investment in these sectors is very important. How much to invest in what sector? This is the major question, which is studied in this topic.

• **Problem of economic growth**

If the productive capacity of the economy grows, it will be able to produce more goods as a result of which the living standard of the people will rise. The increase in productive capacity of an economy is called economic growth. There are various factors affecting economic growth which in turn will affect Business economics.

**FUNDAMENTAL / BASIC CONCEPTS OF BUSINESS ECONOMICS**

Decision making is the core of Business economics. The following are the six fundamental concepts used in Managerial Economics:

1. **Marginalism:**

Marginalism is a theory that attempts to explain the discrepancy in the value of goods and services by reference to their secondary or marginal utility. This was proposed by Adam Smith.
ADAM SMITH struggled with what came to be called the paradox of “value in use” versus “value in exchange.” Water is necessary to existence and of enormous value in use; diamonds are frivolous and clearly not essential. But the price of diamonds—their value in exchange—is far higher than that of water. Smith had failed to distinguish between “total” utility and “marginal” utility. The elaboration of this insight transformed economics in the late nineteenth century, and the fruits of the marginalist revolution continue to set the basic framework for contemporary MICROECONOMICS.

For instance: The total utility or satisfaction of water exceeds that of diamonds. We would all rather do without diamonds than without water. But almost all of us would prefer to win a prize of a diamond rather than an additional bucket of water. To make this last choice, we ask ourselves not whether diamonds or water give more satisfaction in total, but whether one more diamond gives greater additional satisfaction than one more bucket of water. For this marginal utility question, our answer will depend on how much of each we already have. Though the first units of water we consume every month are of enormous value to us, the last units are not. The utility of additional (or marginal) units continues to decrease as we consume more and more.

2. **Equi-marginalism:**

   The principle of equi-marginalism is also called law of equi-marginal utility. The principle of equi-marginal utility explains the behavior of a consumer in distributing his limited income among various goods and services.
This law states that how a consumer allocates his money income between various goods so as to obtain maximum satisfaction. For example, a consumer has Rs.50 with him and he wants to purchase apples and oranges. The cost of each apple is Rs. 5 and orange is Rs.5. he spends his money in such a way that the final satisfaction he gets from spending the last rupee on two products is equal. He purchases 6 units of apple and 4 units of oranges in order to get equal satisfaction. [This particular topic will be discussed in detail in unit 2]

**Equi-marginal Principle Assumptions**

- Utility could be calculated in cardinal numbers.
- Consumer is rational. He desires maximum satisfaction from income. He is influenced by fashion and habits.
- The income of purchaser is steady.
- The prices of products stay constant.
- A good can be split up in small portion. It means that the purchaser can spend his income as he wishes.
- The customer has understanding of the utility offered by different products.
- Utility which a purchaser receives from a product is determined by the quantity of that product only. It’s not at all influenced by the utility resulting from other items.
- Consumption is made at a certain period of time. This implies that the budget period of the purchaser is constant.

### 3. Opportunity cost:

Every scarce goods or activity has an opportunity cost. Opportunity cost of anything is the cost of the next best alternative which is given up. It refers to
the cost of foregoing or giving up an opportunity. It is the earnings that would be realized if the available resources were put to some other use. It implies the income or benefit foregone because a certain course of action has been taken. Thus opportunity costs are measured by the sacrifices made in the decision. If there is no sacrifice involved by a decision there is no opportunity cost. It is also called alternative cost or transfer cost. The opportunity cost of using a machine to produce one product is the income forgone which would have been earned from the production of other products. If the machine has only one use, it has no opportunity cost. Similarly, the opportunity costs of funds invested in one's own business is the amount of interest earned if the amount had been used in other projects. If an old building is proposed to be used for a business, likely rent of the building is the opportunity cost. These are called opportunity costs because they represent the opportunities which are foregone. Devenport, an American Economist explains the concept of opportunity cost with reference to an example. Suppose a girl had two kinds of fruits- one pear and one peach, and if a bad boy is after her to seize the fruits, then the best way for the girl is to drop one fruit and run with the other, so that, she can at least save one fruit, at the cost of the other. When the girl so drops by the way-side one fruit and runs with the other, then the opportunity cost of the fruit she saves is the foregone alternative of the fruit she lost. This is the opportunity cost theory. The concept of opportunity cost plays an important role in managerial decisions. This concept helps in selecting the best possible alternative from among various alternatives available to solve a particular problem. This concept helps in the best allocation of available resources.
4. **Time perspective:**

   Another principle is the principle of time perspective which is useful in decision-making in output, prices, advertising and expansion of business. Economists distinguish between the short run and the long run in discussing the determination of price in a given market forms because in the long run a firm must cover its full cost. On the contrary, in the short-run it can afford to ignore some of its (fixed) costs. Modern economists have started making use of an "intermediate run" between the short run and the long run. The principle of time perspective can be stated as under:

   A decision should take into account both the short run and the long run effects on revenues and costs and maintain a right balance between the long run and the short run perspectives.

5. **Discounting concept:**

   Generally people consider a rupee tomorrow to be worth less than a rupee today. This is also implied by the common saying that a bird in hand is worth than two in the bush. Anybody will prefer Rs. 1000 today to Rs. 1000 next year. There are two main reasons for this:

   (1) The future is uncertain and it is preferable to get Rs. 1000 today rather than a year after;

   (2) Even if one is sure to receive the Rs. 1000 next year, one would do well to receive Rs. 1000 now and invest it for a year and earn a rate of interest on Rs. 1000 for one year.

   The formula for computing present value of money is
Present value = \( A / (1 + i)^n \)

Where, \( A \) = amount invested or interested in

\( I \) = rate of interest and \( n \) = number of years.

Suppose you shall receive 1000 next year from your friend, then the present value is

\[
\text{Present value} = \frac{1000}{(1 + 10\%)^1} \\
= 1000/1.1 \\
= \text{Rs. 909.}
\]

It can be explained as "If a decision affects costs and revenues at future dates, it is necessary to discount those costs and revenues to obtain the present values of both before a valid comparison of alternatives can be made".

6. **Risk and uncertainty:**

The future is uncertain and involves risk. The uncertainty is due to unpredictable changes in the business cycles and the environment in which business operates. This means management must assume some risk when making decisions. Economic theory generally assumes that the firm has perfect knowledge of its costs and demand relationships and of its environment. Uncertainty is not allowed to affect the decisions. Uncertainty arises because producers cannot foresee the dynamic changes in the economy.
7. Efficiency:

The term efficiency refers to the use of resources so as to maximize the production of goods and services. An economic system is said to be more efficient than another if it can provide more goods and services for society without using more resources.

Economic efficiency occurs when the cost of producing a given output is as low as possible. It depends on the process of the factors of production. Something that is technologically efficient may not be economically efficient. But something economically efficient is always technologically efficient.

One should consider the assumptions of dealing with efficiency. That is Ceteris paribus (all other things remain constant). When dealing with decisions involving minimum cost for given output, except cost all the other things must be constant.

8. Externality and tradeoff:

Externality refers to the consequence of an economic activity that is affected by unrelated third parties. An externality can be either positive or negative. All the factors like political, economic, socio-cultural, technological, environmental and legal comprise externality. Externalities can be measured by comparing planned production output with actual output.

Tradeoff: A technique of reducing or forgoing one or more desirable outcomes in exchange for increasing or obtaining other desirable
outcomes in order to maximize the total return or effectiveness under given circumstances. When reviewing multiple opportunities with limited resources, companies frequently compare the tradeoffs of each and then select the opportunities that will yield the highest benefit, while opting not to perform the others, or to perform them at a later time.

9. Others

a. Principle of incremental cost and revenue:

Two important incremental concepts are incremental cost and incremental revenue. Incremental cost is a change in total cost resulting from a decision. Incremental revenue means the change in total revenue resulting from a decision.

A decision is profitable only if

(i) It increases revenue more than costs,

(ii) It decreases some costs more than it increases others,
(iii) It increases some revenue more than it decreases others, and
(iv) It reduces costs more than revenue.

Incremental principle can be used in the theories of consumption, production, pricing and distribution. Incremental concept is closely related to marginal cost and marginal revenue in the theory of pricing.

OPTIMISATION

Definition:

“Finding an alternative with the most cost effective or highest achievable performance under the given constraints, by maximizing desired factors and minimizing undesired ones.”

In comparison, maximization means trying to attain the highest or maximum result or outcome without regard to cost or expense. Practice of optimization is restricted by the lack of full information, and the lack of time to evaluate what information is available. In computer simulation (modeling) of business problems, optimization is achieved usually by using linear programming techniques of operations research.

Optimization in economics simply refers to the actions by which individual economic agents do as well as they can. Firms seek to maximize profits with given production level and inputs or they seek to minimize cost with given output level.

Optimization basically uses mathematical models. Linear programming is the widely used optimization technique.
Business units when using optimizing model have to determine the objective function (their choice either to minimize cost or maximize profit) and the factors that affect their objectives & analysis. The factors that affect (restrict) the decision are called constraints. Thus, certain optimization models have constraints and other may not have. By this we can divide optimization models into constrained and unconstrained models.

**UNCONSTRAINED AND CONSTRAINED OPTIMIZATION**

1. An unconstrained optimization problem is one where you only have to be concerned with the objective function you are trying to optimize and there will be no constraints. An objective function is a function that you are trying to optimize.

   Example: Production of fans with unlimited a flexible budget, where the investment can be increased if more fans have to be produced.

2. In Constrained optimization, a firm cannot hire more than a certain amount of resources due to various limitations. Their production is determined by the factors of production which are fixed in quantity and cannot be increased flexible if the firm wants to increase the output.

   Examples: Individuals maximizing utility will be subject to a budget constraint.

   Firms maximising output will be subject to a cost constraint.
ECONOMICS OF INFORMATION

Information economics or the economics of information is a branch of microeconomic theory that studies how information and information systems affect an economy and economic decisions. Information has special characteristics. It is easy to create but hard to trust. It is easy to spread but hard to control. It influences many decisions. These special characteristics (as compared with other types of goods) complicate many standard economic theories.

GENERAL ECONOMIC PROPERTIES OF INFORMATION

1. While information is represented in physical form, that form can be changed without changing its content.

2. In contrast to physical goods, intellectual goods can be created with limited physical resources, and frequently as a by-product of other operations.

3. Information is easily and cheaply transported. The first copy represents most of the costs in creation, and reproduction costs are relatively small. As a result, it that can be produced and distributed with minimal depletion of physical resources.

4. There is an evident and direct relationship between physical goods and the materials used in producing them. One knows exactly how much steel is needed to produce a car. But there is no comparably direct relationship between any kind of good — physical or symbolic — and the information used in its production. The value of research, market information, or advertising is uncertain, at best probabilistic, and much of the value is potential rather than actual.
5. There is a complex relationship between the time of acquiring information and the value of it. For some, the value lies in immediacy—yesterday's stock information may be worthless tomorrow. For others, the value is likely to be received in the future rather than the present.

6. Persons differ greatly in perceptions of the value of information, in kinds of use, in ability and willingness to use, in assessments of costs, and in ability to pay. Typically the distribution of use of information is highly skewed, with small percentages of users frequent in their use and the great majority infrequent.

7. Use of information is affected by the distance users must travel to get access to it. The theory states that the use of any facility decays as the distance increases, as a function of the cost of travel; if the cost is linear, the decay is exponential and if the cost is logarithmic, it is quadratic. This theory applies to information resources.

8. An accumulation of information has more value than the sum of the individual values because it increases the combinations that can be made. The information technologies have greatly increased the ability to make combinations. The number of databases, their size, the means for processing and relating them, the ability to use them—all are growing exponentially.

9. There are immense economies of scale. Combined with the value in accumulation, this provides strong incentives for sharing information, especially since, once available, it can be distributed cheaply, which makes sharing easy.
10. Information is not consumed by being used or transmitted to others. It can be resold or given away with no diminution of its content. Many persons may possess and use the same information, even at the same time, without diminishing its value to others. All these imply that information is a public good.

11. However, there is the need to invest in the creation, production, and distribution of information and that implies a wish to recover the investment. Furthermore, there may be value associated with exclusivity in knowledge, so there must be an incentive to make it available to others. This implies that information is a private good.

**THE MACRO ECONOMICS OF INFORMATION**

1. The macro-economics of information relates to its role in national economies, as reflected in the distribution of the workforce among various types of activities and functions. It also relates to effects on national economic policies.

**THE MICRO ECONOMICS OF INFORMATION**

1. Income to the providers of information.
2. The costs of information
3. The value of information.
**Extra topics (may be asked for external)**

**ROLE OF A BUSINESS ECONOMIST**

A Business economist plays a vital role in modern business. He helps the management of a firm in decision making and forward planning by using his skills and techniques. In advanced countries like U.S.A., U.K. and Canada, almost all big firms employ managerial/business economists. Tata, Hindustan Lever and Reliance have business economists on their staff. The role of a business economist is that of a business analyst and of an advisor. It is a part and parcel of modern business activities. Accordingly, his responsibilities are also heavy.

1. **Study of the business environment:**

   Every firm has to take into consideration such external factors as the growth of national income, volume of trade and the general price trends, for its policy decision. A firm works within a business environment. The basic elements of business environment of a firm are the trend of growth of national economy and world economy and phase of the business cycle in which the economy is moving. At what rate and where is population getting concentrated? Where are the demand prospects for established and new products? Where are the prospective markets? These questions lead the
economists into purposeful studies of the economic environment. The international economic outlook is a very important environmental factor for exporting firms. The nature and degree of competition within the industry in which a firm is placed are also a part of the business environment. The kind of economic policies pursued by the government constitute a powerful element of the business environment of a firm. What are the priorities of the new five year plan? In which sectors of the economy have the outlays been bran increased? What are the budgetary trends? What about changes in expenditure, tax rates tariffs and import restrictions? For all purposes the economists place a significant role.

2. Business Plan and Forecasting:

The business economists can help the management in the formation of their business plan by forecasting and economic environment. The management can easily decide the timing and locating of their specific action. The business economist has to interpret the national economic trends and industrial outlook for their relevance to the firm in which he is working. He advises top management by means of short, business like practical notes. In a partially controlled economy like India, the business economist translates the government's intentions in business jargon and also transmits the reaction of the industry to propose changes in government policy.

3. Study of business operations:

The business economist can also help the management in decision making relating to the internal operations of a firm, i.e., in deciding about price, rate of operations, investment and growth of the firm for offering this advice; the economist has specific analytical and forecasting techniques which yield meaningful conclusions. What will be the reasonable sales and profit budget
for the next year? What are the suitable production schedules and inventory policies? What changes in wage and price policies are imperative now? What would be the sources of finance? Thus, he is trained to answer such questions posted by the top management.

4. **Economic intelligence:**

The business economist also provides general intelligence services by supplying the management with economic information of general interest so that they can talk intelligently in conferences and seminars. They are also supplied the facts and figures for preparing the annual reports of the firm. Those facts and figures are collected by the business economist as he understands the literature available on business activities.

5. **Specific functions:**

Business economists are now performing specific functions as consultants also. Their specific functions are demand forecasting, industrial market research, and pricing problems of industry, production programmes, investment analysis and forecasts. They also offer advice on trade and public relations, primary commodities and foreign to capital projects in agriculture, industry, transport and tourism and also of the export environment. 6. **Participation in Public Debates.** The business economists participate in public debates organized by different agencies. Both governments and society seek their advice. Their practical experience in business and industry gives value to their observation. In nutshell a business economist can play a multi-faceted role. He is not only an analyst of current trends and policies for his employers but also a bridge between the businessmen in the specific industry and the Govt.
RESPONSIBILITIES OF A BUSINESS ECONOMIST

A business economist is well familiar with his responsibilities. He must keep in the mind the main objective of making a reasonable profit on the invested capital in his firm. Firms are not always after profit-maximization, but to continue in business, every firm has to operate for profit. Therefore, a business economist has the main responsibility of helping the management to make more profits than before. All his other responsibilities flow from this basic obligation.

The responsibilities of a business economist are summarized below:

1. Making successful Forecasts:
   Managements have to take decisions concerning the future and it is uncertain. This uncertainty cannot be eliminated altogether but it can be reduced through scientific forecasts of the economic environment to his employers. This is required for business planning. If a business economist can make successful forecasts about business trends, the management will hold him in great esteem. A wise Business Economist will revise his forecasts from time to time keeping in view new developments in his business. As soon as he finds a change in his forecasts, he has to alert the management about it. He assists the management in making the needed adjustments. This will help him to strengthen his position as a member of the managerial team.

2. Maintaining Relationships:
   The Business Economist must establish and maintain contacts with data sources for his analysis and forecasts. He makes contacts with individual who are specialists in the different fields. He must join professional associations and subscribe to the journals giving him fresh and latest
information. In other words, his business biggest quality is his ability to obtain information quickly by establishing contacts with the sources of such information.

3. **Earning full Status on the Managerial team:**

A Business Economist has to participate in decision-making and forward-planning. For this he must be able to earn full status on the business team. He must be prepared to take up assignments on special project also. He should be able to express himself clearly so that his advice is understood and accepted. Finally, he must be in tune with the industry's thinking, and not lose the national perspective in giving advice to the management. Thus, we can conclude from our discussion that Business Economists can earn an important place in the managerial team only if the understands and undertakes his responsibilities.

**BUSINESS ECONOMICS AND OTHER DISCIPLINES**

To broadly appreciate the nature and scope of Business Economics it is necessary to examine its relationship with other sciences. At this juncture it is apt to specially mention the relationship of Business Economics with the important fields of study such as statistics, mathematics, operations research, and accounting.

**Business Economics and Statistics**

Statistics provides several tools to Business Economics; Statistical techniques are used in collecting, marshalling and analyzing business data that makes possible an empirical testing of the economic generalizations before they are applied for decision making. Economic generalizations cannot be fully accepted until they are verified and found Valid against the real data. The theory of probability and
forecasting techniques help the manager in decision-making process. When the manager is to meet with the reality of uncertainty in decision making the theory of probability provides the logic for dealing with such uncertainty.

**Business Economics and Mathematics**

Mathematics is especially of to the manager when several economic relationships are to logic in the analysis of economic events provides clarity of the concepts and also helps to establish a quantitative relationship. Managers deal primarily with concepts that are quantitative in nature eg., demand, price, cost, capital, wages, inventories etc. Mathematics is the manager's most useful logical tool. Techniques such as linear programming, matrices, and equations are widely used.

**Business Economics and Operations Research**

Operation research and managerial economics are related to a certain extent. Operation research is the application of mathematical and statistical techniques in solving business problems. It deals with construction of mathematical models that helps the decision making process. Operation research is helpful in business firms in studying the inter-relationship and relative efficiencies of various business aspects like sales, production etc. Linear programming, techniques of inventory control, game theory etc., are used in Business Economics. These are used to find out the optimum combination of various factors to achieve the objects of maximization of profit, minimizations of cost and time etc.
Business Economics and Accounting

Accounting is closely related with Business Economics. Accounting is the main source of data regarding the operation and functioning of the firm. Accounting data and statements represent the language of the business. A business manager needs market information, production information and accounting information for decision-making. The profit and loss statement reflects the operational efficiency of the firm. The balance sheet tells the financial position of the firm. The accounting information provides a basis for the manager in decision making and forward planning. In short, accounting provides right information to take right decisions.

IMPORTANCE / SIGNIFICANCE OF BUSINESS ECONOMICS

Theoretical:

- Understanding Economic Behaviour
- Intellectual Value
- Economic Tools
- Economic Growth
- Economic Development
- Economic Planning
- Prediction
- Ethical Values
- Economic Performance Measurement
Unit 1 – Introduction to Business Economics | BBA I year

Practical:

- Useful To Finance Minister
- Useful In Planning
- Useful To Bankers
- Trade Unions
- Businessmen
- Statesmen
- International Economics

Probable questions:

SHORT

Define

a) scarcity  b) choice  c) opportunity cost  d) business economics  e) cost analysis  
f) prescriptive economics  g) normative science  h) marginalism  i) eau-marginalism  
j) discounting principle  k) risk  l) uncertainty  m) externality and tradeoff  n) optimization  
op) micro economics  p) macro economics.

LONG

1. What is business economics? Explain its importance.
2. “Business economics is the crux of decision making” explain.
3. Explain the basic economic problems.
4. Explain the importance of opportunity coat in decision making.
5. What are the objectives of business economics?
6. Business economics is an art as well as science. Which one do you support? Justify.

7. Role of business economist in an organization.

8. Business economics has its own limitations. Comment.

9. What is optimization? What is the importance of optimization?


12. Scope of business economics.

13. Explain the role and responsibility of business economist in the globalized world.

14. Any other question. But the subject matter would be the same.