

Module:

01

**Introduction to Business
Economics**

Content:

-) Meaning, Nature and Scope of Business Economics.
-) Distinctions between Economics and Business Economics.
-) Importance of Business Economics.
-) Basic Problems of an Economy and Role of Price Mechanism.
-) Features of Free Market Economy and Price Mechanism.

➤ What is Business Economics?

Business Economics is the integration of economic theory with business practice for the purpose of facilitating decision making and forward planning by management.

Business Economics, also referred to as Managerial Economics, generally refers to the integration of economic theory with business practice.

Managerial economics is concerned with the application of economic concepts and economics to the problems of formulating rational decision making.

> Nature of Business Economics

1. Microeconomics
2. Macroeconomics
3. Business Economics is a Science (Social Science)
4. Business Economics is an Art
5. Business Economics is Normative science
6. Business Economics is Positive Science
7. Business Economics is Pragmatic Science
8. Business Economics is Prescriptive
9. Management oriented

> Scope of Business Economics

The scope of business economics is quite wide. Business economics involves the application of various economic tools, theories, and methodologies for analyzing solving different business problems.

Two Categories:

There are two categories of business issues to which economic theories can be directly applied, namely:

- . Microeconomics applied to internal or operational issues
- . Macroeconomics applied to external or environmental issues.

> Difference Between Economics and Business Economics

ECONOMICS	BUSINESS ECONOMICS
Economics is a traditional subject that has prevailed from a long time.	Business economics is a modern concept and is still developing.
Economics mainly covers theoretical aspects.	Business economics covers practical aspects.
In economics, the problems of individuals and societies are studied.	In Business economics, the main area of study is the problems of organizations.
In economics, only economic factors are considered.	In business economic, both economic and non-economic factors are considered.

➤ Importance of Business Economics

Business economics plays an important role in decision making in an organisation. Decision making is a process of selecting the best course of action from the available alternatives. Role and responsibilities of managerial economics are explained below.

The following points explain the **importance of business economics**:

1. Identifying, analyzing problems and finding solutions
2. Identify, analyze various internal & external business factors
3. Framing various policies
4. Predict the future
5. Establishing relationships between different economic factors

Basic Problems of an Economy and Role of Price Mechanism:

Basic problems of an Economy:

- What to Produce
- How to Produce
- For whom to Produce.
- Allocation of scarce resources.

Price mechanism :

Introduction:

- *PRICE MECHANISM* is an economic term that refers to the manner in which the price of commodities affect to demand & supply of good & services.
- Price mechanism affects both buyers & sellers who negotiate prices of goods or services.
- A price mechanism or market-based mechanism refers to a wide variety of ways to match up buyers & sellers through price rationing.

What is price mechanism ?

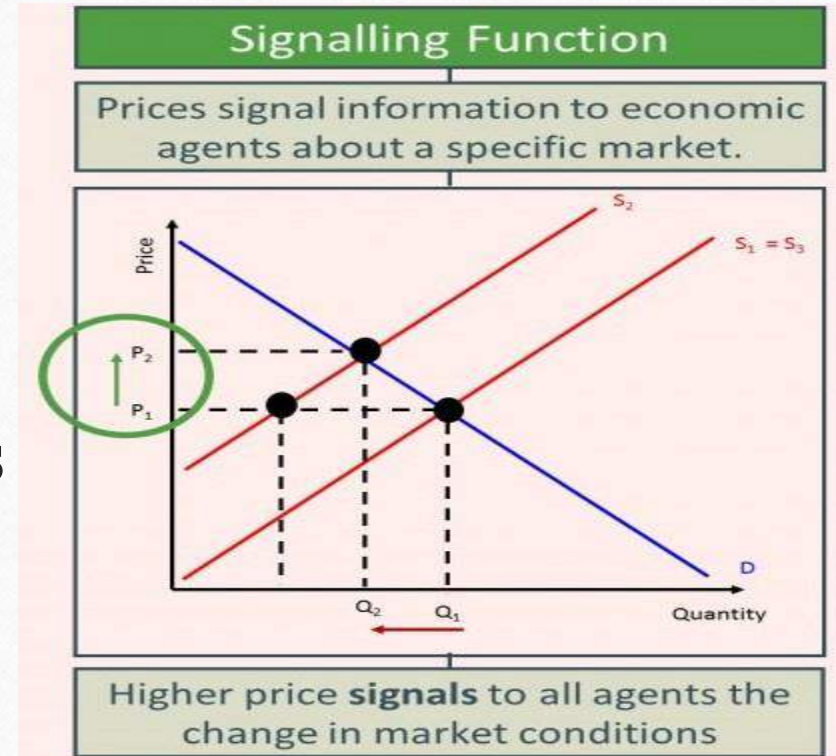
- Price mechanism is also known as market mechanism.
- The price mechanism is the means by which decisions of consumers & businesses interact to determine the allocation of resources .
- The free market price mechanism clearly does **not** ensure an equitable distribution of resources & can lead to market failure .

Functions of Price mechanism

1. Signalling Functions
2. Incentives Functions
3. Rationing Functions

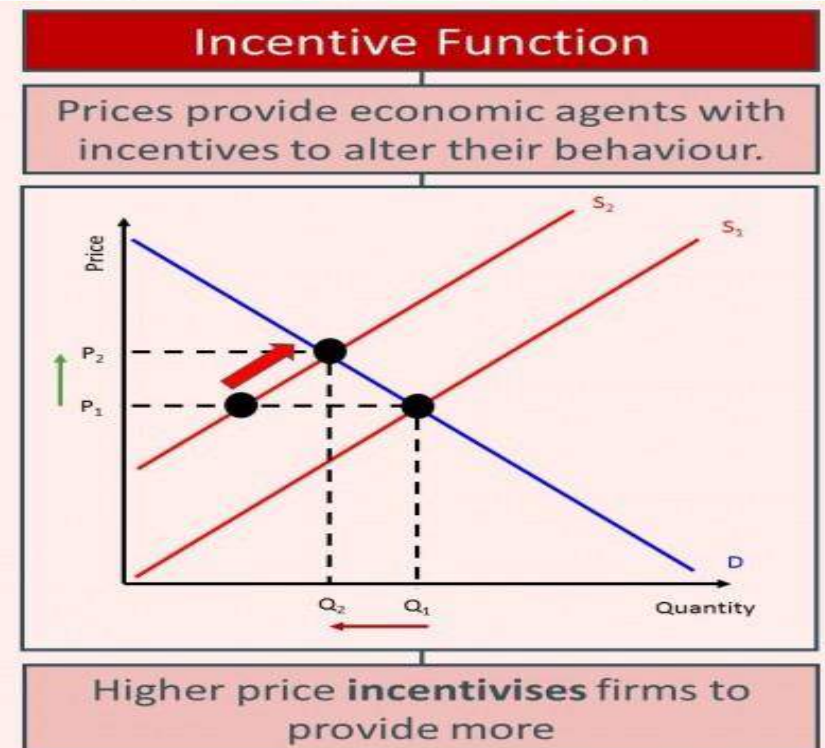
Signalling Functions

- Market prices adjust to demonstrate where resources are required, & when they are not.
- Prices rise & fall reflect scarcities & surpluses.



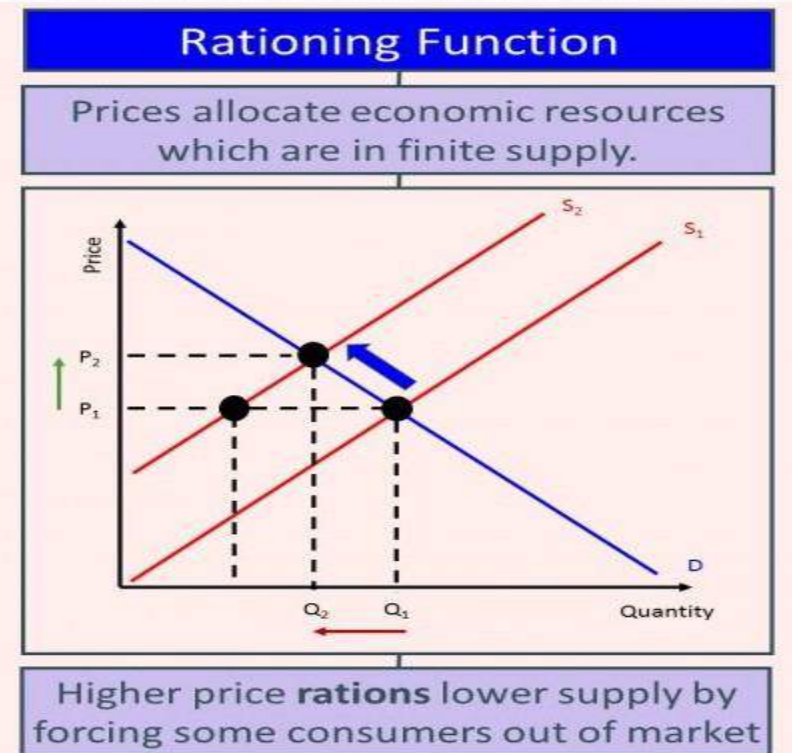
Incentives functions

- When the price of a product rises, the quantity supplied increases, this is due to the incentives functions.



Rationing function

- Price rations scarce resources when demand outstrips supply .
- When there is a shortage , price is bid up – leaving only those with willingness & ability to pay to buy .



Effect of Price Mechanism

- Price mechanism causes many changes in economic environment . if there is an increase in demand , then prices will go higher causing a movement along the **supply curve**.

Examples for price mechanism

- ☐ **Example of price mechanism in the long term is the oil crisis during the 1970s .**
- ☐ **The crisis caused more nations to start producing its own oil due to dramatic price increases of oil .**
- ☐ **Since more nations started to produce oil , the supply curve shifted more to the right meaning there was more supply of oil .**

➤ Summary of Business Economics

Business Economics comprises of that part of economic knowledge, logic, theories and analytical tools that are used for rational business decision making. In brief, it is Applied Economics that -fills the gap between economic theory and business practice.

