

The firm and perfect market structure

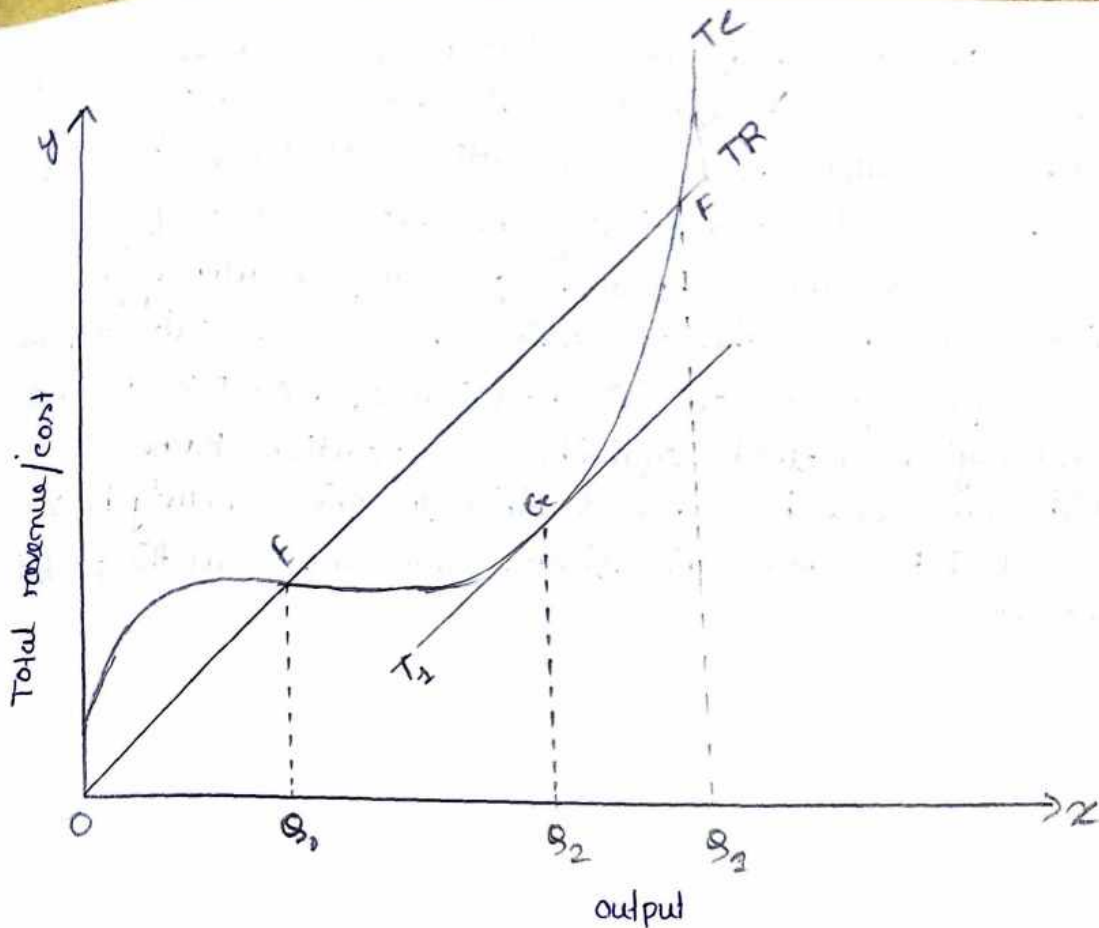
① Briefly discuss the behaviour of profit maximising firms under the condition of perfect market structure?

OR
How does profit determine by a firm with $TR-TC$ approach and $MR-MC$ approach? under market structure?

OR
Briefly discuss the mechanism of determination of maximum profit for a firm on the basis of market oriented production process? 10

Ans Generally each and every firm under any market structure have the major objective to earn profit. For earning profit, the firm should follow such type of production process which minimises cost and maximises revenue. Basically the emergent difference between total revenue (TR) and total cost (TC) is called profit. Therefore in the behaviour of profit maximising firm and its production process, there are two approaches to determine maximum profit which can be stated as follows —

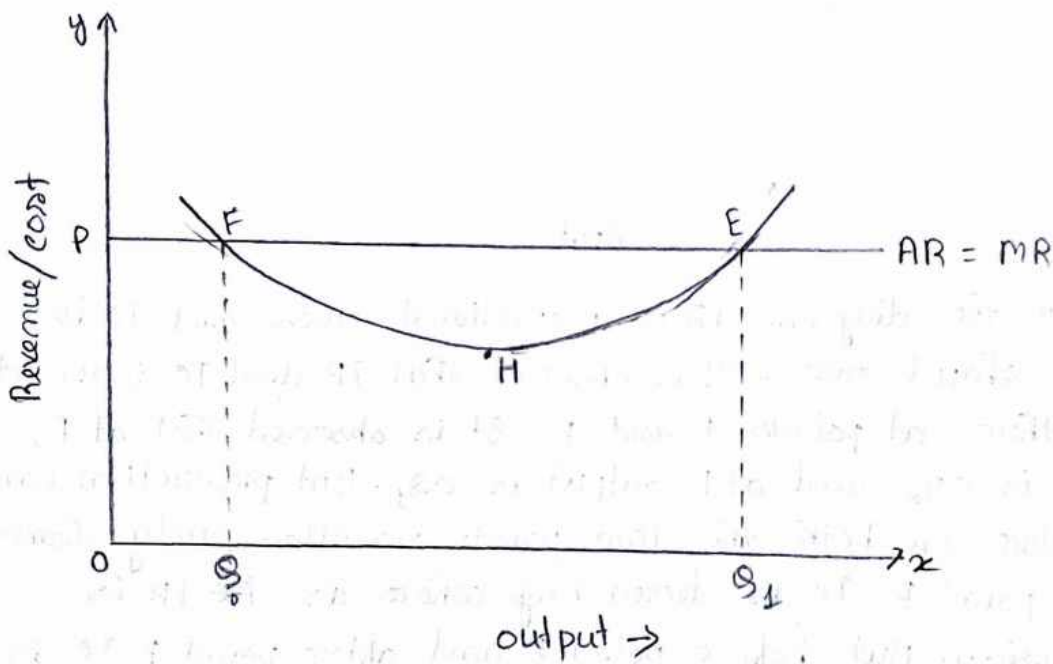
① $TR-TC$ approach :- Generally profit under perfect market structure can be determine with the existing differences between TR and TC in the process of production. Since under perfect competition price is fixed, therefore increase in output leads to increase in TR . Under such a situation, TR curve will become proportional. With the proportional TR , the corresponding TC of production can determine profit for the firm. Such determination process can diagrammatically be explained as follows —



In the diagram TR is proportional curve and TC is different shaped curve. It is observed that TR and TC intersects each other at points E and F. It is observed that at E, output is OQ_1 and at F output is OQ_3 . But production cannot take place in both the two points simultaneously. Generally after point E TC is decreasing where as TR is increasing. But before point E and after point F, TC is higher than TR. Therefore production cannot take place before E and after F. In the diagram at point G, the line T_1 is tangent which is become parallel to TR. Therefore at G, profit is maximum where OQ_2 is the output. But, G cannot be the equilibrium. Rather equilibrium will be at F where TC cuts TR from below. At point F the firm will be equilibrium by producing OQ_3 output where all the profit shown by the area EGF can be earned.

⑩ MR-MC approach - A firm under perfect market structure can be determine profit π on the basis of MR-MC approach. Basically the determination of profit by this approach can diagrammatically be explained as follows -

In this approach, generally equilibrium position can be achieved when MC curve cuts ^{MR} from below. Generally at all the position of $MC = MR$ does not necessarily $\&$ implied equilibrium position. Rather equilibrium will be achieved through the equality between MC and MR when the firm can earn all the profit amount.



In the diagram MC $\&$ cuts MR from ^{above and} below at points F and E. Basically since under perfect competition, price of all the units of the commodity is fixed, therefore price = AR = MR. At point F the firm produces Q_0 output from which cost is decreasing and even MC is minimum at point H, and after that it is increasing. But at point E the firm can produce Q_1 output at where MC cuts MR from below and after E point MC is more than MR. Therefore equilibrium point cannot

be left of F and right of E. Rather it should be E as at E, the firm can earn all the existing amount of profit shown by FHE area in the diagram.

9. What do you mean by perfect competition? What are the characteristic features of perfect competition?

Ans Perfect competition is defined as such a market structure in which very large number of buyers and sellers are involved for buying and selling a perfect homogeneous product on the basis of free and free and exit. Therefore under such type of market each and every buyer and seller plays an important role for buying and selling of the product.

There exists certain characteristic feature of perfect competition which can be stated as follows —

- (i) Under perfect competition, one of the important characteristic feature is that there exist a very large number of buyers and sellers. It should be noted that the role of or the contribution of each and every buyer and seller in the market is insignificant. ~~Another~~
- (ii) Another characteristic of perfect competition is considered as perfect homogeneity of the product. It implies that each and every unit of the product in the market is identical. Therefore it becomes difficult to search different prices of the product at the same point.
- (iii) Another characteristic of such a market structure is there is no restriction of ~~and~~ entry and exit of firms in the market or from the market.
- (iv) As a result of such entry and exit policy all the firms in the market can earn only normal profit.

in the long run.

(iv) Under perfect competition, all the buyers and seller have perfect knowledge about the market conditions. The seller must know the prices being charged by other firms in the market. Even the buyers must know the prices being charged by different prices.

(v) Another characteristic of perfect competition is that all the firms have equal access to the market. It implies that while transporting a commodity from one place to another, the firms had not incurred in any cost.

Q. What are the differences between firm and industry?

Ans A firm is defined as an independent unit of producing goods and services sells. Generally a firm taken as a production unit producing an output. A firm is in equilibrium when it maximises profit by satisfying the condition of equality between MC and MR production.

On the other hand, an industry is defined as a combination of firms producing homogeneous product in the market. Generally an industry is an independent entity of homogeneous product producing firms. An industry is in equilibrium when there is no tendency of ~~a firm~~ ^{on the part} of any firm in the industry to go out or for any firm from out of it to enter.

Q. How does equilibrium price in an industry determine? Explain the role of that price for determining AR of the firm in perfect competition?

OR