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ANSWER NO.1

1. Benefit principle:

The benefit principle is the idea that government spending should be met by the people who receive them. In other words, everyone who receives government spending, should contribute towards it.

This benefit principle was the justification for Margaret Thatcher's Poll Tax. Everyone was charged the same poll tax rate because the argument was that everyone benefited from the same public services.

In practice the benefit principle is hard to apply because many of those in need of government benefits – the old, sick and unemployed are the least likely to be able to pay. A general principle more commonly used is the ability to pay.

2. Lump-Sum Tax:

A tax in which the taxpayer is assessed the same amount regardless of circumstance. An example of a lump-sum tax is a \$55 fee on all employees who work in a township. Another example is tag fees on vehicles, which are the same regardless of the income of vehicle owners. Lump-sum taxes are regressive, meaning persons with lower income pay more as a percentage of their income.

3. Marginal tax rate verses Average Tax rate:

Average tax rates measure tax burden, while marginal tax rates measure the impact of taxes on incentives to earn, save, invest, or spend.

Average tax rates are a measure of a household's tax burden; that is, how taxes affect the household's ability to consume today or (through saving) in



the future. Marginal rates measure the degree to which taxes affect household (or business) economic incentives such as whether to work more, save more, accept more risk in investment portfolios, or change what they buy. Higher marginal rates reduce incentives to engage in a particular activity (such as work) or (in the case of sales taxes) consume a particular item.

4. Proportional Tax:

A proportional tax is an income tax system that levies the same percentage tax to everyone regardless of income. A proportional tax is the same for low, middle, and high-income taxpayers. Proportional taxes are sometimes referred to as flat taxes.

In contrast, a progressive tax or marginal tax system adjusts tax rates progressively by income. Low-income earners are taxed at a lower rate than high-income earners.

5. Regressive Tax:

A regressive tax is a tax applied uniformly, taking a larger percentage of income from low-income earners than from high-income earners. It is in opposition to a progressive tax, which takes a larger percentage from high-income earners.

6. Progressive Tax:

A progressive tax is a tax that imposes a lower tax rate on low-income earners compared to those with a higher income, making it based on the taxpayer's ability to pay. That means it takes a larger percentage from high-income earners than it does from low-income individuals.



ANSWER NO.2

Elasticity:

Elasticity is a measure of a variable's sensitivity to a change in another variable, most commonly this sensitivity is the change in price relative to changes in other factors. In business and economics, elasticity refers to the degree to which individuals, consumers or producers change their demand or the amount supplied in response to price or income changes. It is predominantly used to assess the change in consumer demand as a result of a change in a good or service's price.

1. Income Elasticity of Demand:

Income elasticity of demand refers to the sensitivity of the quantity demanded for a certain good to a change in real income of consumers who buy this good, keeping all other things constant.

The formula for calculating income elasticity of demand is the percent change in quantity demanded divided by the percent change in income. With income elasticity of demand, you can tell if a particular good represents a necessity or a luxury.

2. Price Elasticity of Demand:

Price elasticity of demand is an economic measure of the change in the quantity demanded or purchased of a product in relation to its price change. Expressed mathematically, it is:

Price Elasticity of Demand = % Change in Quantity Demanded / % Change in Price

Price elasticity is used by economists to understand how supply or demand changes given changes in price to understand the workings of the real economy. For instance, some goods are very inelastic, that is, their prices do not change very much given changes in supply or demand.



Examples of Price Elasticity of Demand:

Generally as rules of thumb, if the quantity of a good demanded or purchased changes more than the price change, the product is termed elastic. (The price changes by +5% , but the demand falls by - 10%). If the change in quantity purchased is the same as the price change (say, $10\% / 10\% = 1$), the product is said to have unit (or unitary) price elasticity. Finally, if the quantity purchased changes less than the price (say, -5% demanded for a +10% change in price), then the product is termed inelastic.

To calculate the elasticity of demand, let's take a very simple example: Suppose that the price of apples falls by 6% from \$1.99 a bushel to \$1.87 a bushel. In response, grocery shoppers increase their apple purchases by 20% . The elasticity of apples would thus be: $0.20 / 0.06 = 3.33$ indicating that apples are quite elastic in terms of their demand.

3. Cross Elasticity of Demand:

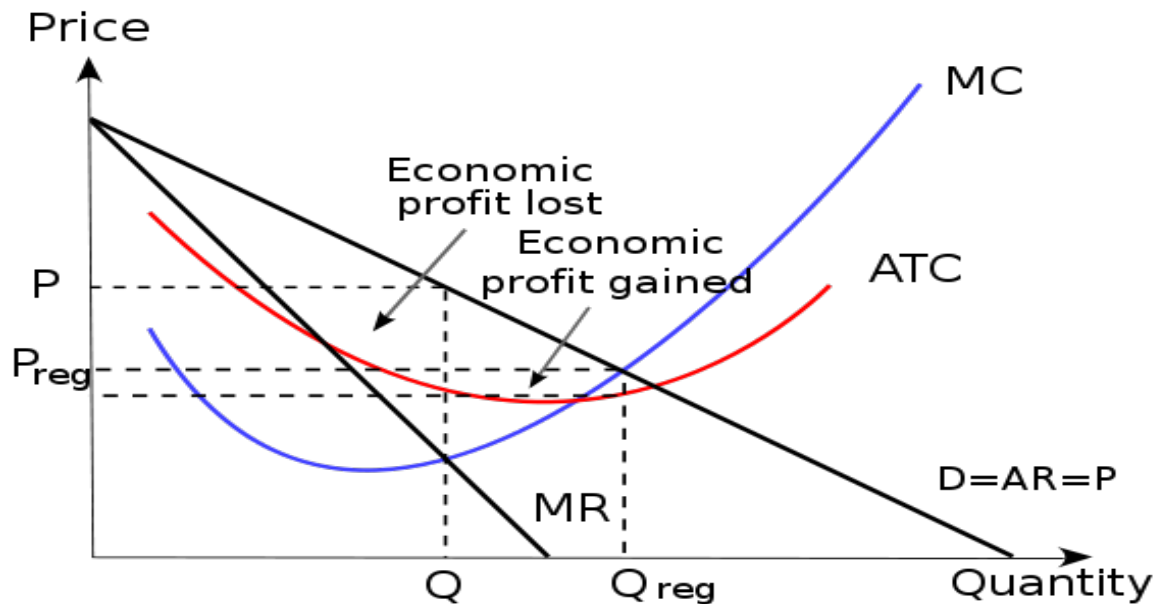
The cross elasticity of demand is an economic concept that measures the responsiveness in the quantity demanded of one good when the price for another good changes. Also called cross-price elasticity of demand, this measurement is calculated by taking the percentage change in the quantity demanded of one good and dividing it by the percentage change in the price of the other good.



ANSWER NO.3

Monopoly:

A monopoly is a specific type of economic market structure. A monopoly exists when a specific person or enterprise is the only supplier of a particular good. As a result, monopolies are characterized by a lack of competition within the market producing a good or service.



Monopoly: The graph shows a monopoly and the price (P) and change in price (P_{reg}) as well as the output (Q) and output change (Q_{reg}).



Characteristics of a Monopoly:

A monopoly can be recognized by certain characteristics that set it aside from the other market structures:

Profit maximizer: a monopoly maximizes profits. Due to the lack of competition a firm can charge a set price above what would be charged in a competitive market, thereby maximizing its revenue.

Price maker: the monopoly decides the price of the good or product being sold. The price is set by determining the quantity in order to demand the price desired by the firm (maximizes revenue).

High barriers to entry: other sellers are unable to enter the market of the monopoly.

Single seller: in a monopoly one seller produces all of the output for a good or service. The entire market is served by a single firm. For practical purposes the firm is the same as the industry.



B.Price discrimination:

in a monopoly the firm can change the price and quantity of the good or service. In an elastic market the firm will sell a high quantity of the good if the price is less. If the price is high, the firm will sell a reduced quantity in an elastic market.

Price Determination under Monopoly:

Monopoly is that market form in which a single producer controls the whole supply of a single commodity which has no close substitute.

A firm under monopoly faces a downward sloping demand curve or average revenue curve. Further, in monopoly, since average revenue falls as more units of output are sold, the marginal revenue is less than the average revenue. In other words, under monopoly the MR curve lies below the AR curve.

The Equilibrium level in monopoly is that level of output in which marginal revenue equals marginal cost. The producer will continue producer as long as marginal revenue exceeds the marginal cost. At the point where MR is equal to MC the profit will be maximum and beyond this point the producer will stop producing.



ANSWER NO.4

A.The Cournot Model:

The Cournot model of oligopoly assumes that rival firms produce a homogenous product, and each attempts to maximize profits by choosing how much to produce. All firms choose output (quantity) simultaneously. The basic Cournot assumption is that each firm chooses its quantity, taking as given the quantity of its rivals. The resulting equilibrium is a Nash equilibrium in quantities, called a Cournot (Nash) equilibrium.

The Cournot model provides results which are of some importance to industrial economics. First of all, it can be shown that price will not in most cases equal marginal costs (see costs) and Pareto efficiency is not achieved. Moreover, the degree to which each firm's price exceeds marginal cost is directly proportional to the firm's market share and inversely proportional to the market elasticity of demand.

If the oligopoly is symmetric, that is, all firms have identical products and cost conditions, then the degree to which price exceeds marginal cost is inversely related to the number of firms.



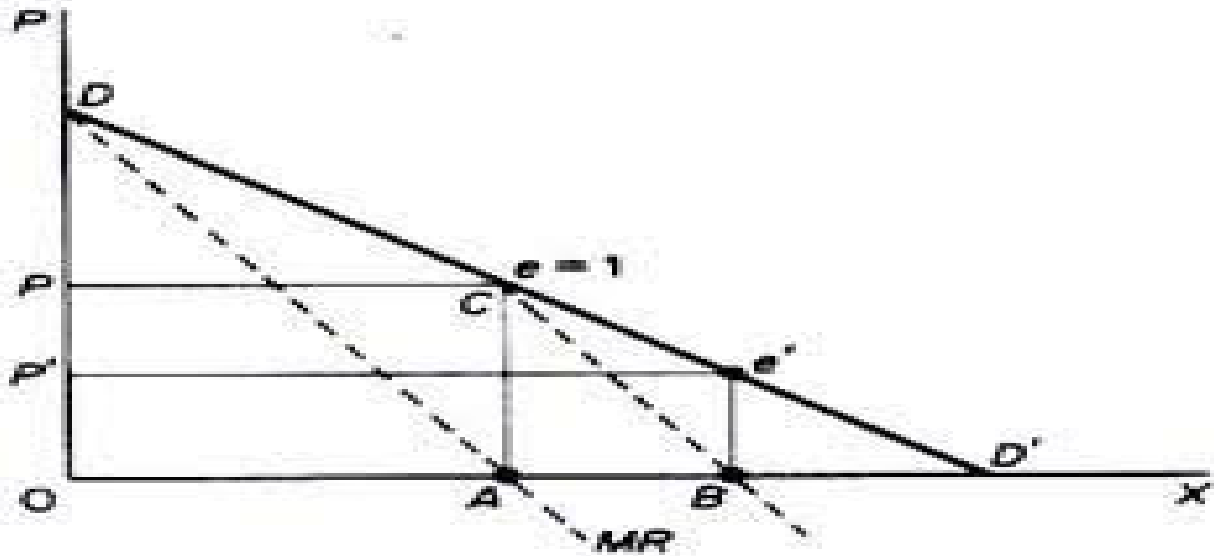
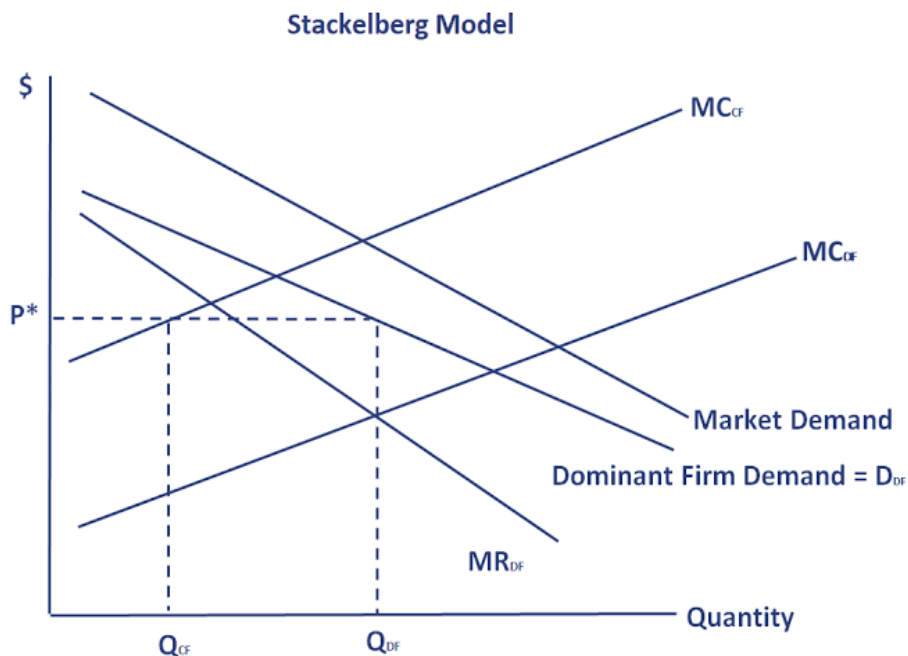


Figure 9.1

B. Stackelberg leadership model :

It is a strategic game in economics in which the leader firm moves first and then the follower firms move sequentially. It is named after the German economist Heinrich Freiherr von Stackelberg who published Market Structure and Equilibrium (Marktform und Gleichgewicht) in 1934 which described the model.

In game theory terms, the players of this game are a leader and a follower and they compete on quantity. The Stackelberg leader is sometimes referred to as the Market Leader.



It can be seen from the diagram that up till OM output, marginal revenue is greater than marginal cost, but beyond OM the marginal revenue is less than marginal cost. Therefore, the monopolist will be in equilibrium at output OM where marginal revenue is equal to marginal cost and the profits are the greatest. The corresponding price in the diagram is MP' or OP. It can be seen from the diagram at output OM, while MP' is the average revenue, ML is the average cost, therefore, P'L is the profit per unit. Now the total profit is equal to P'L (profit per unit) multiply by OM (total output).

In the short run, the monopolist has to keep an eye on the variable cost, otherwise he will stop producing. In the long run, the monopolist can change the size of plant in response to a change in demand. In the long run, he will make adjustment in the amount of the factors, fixed and variable, so that MR equals not only to short run MC but also long run MC.

(The End)