Foundamentals of Economics & Management

Paper - 1

THE INSTITUTE OF COST ACCOUNTANTS OF INDIA

(Statutory body under an Act of Parliament)

www.icmai.in

SYLLABUS - 2016

WORK BOOK

FUNDAMENTALS OF ECONOMICS AND MANAGEMENT

FOUNDATION

PAPER – 1

The Institute of Cost Accountants of India

(Statutory body under an Act of Parliament)

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First Edition : March 2019

Published By :

Directorate of Studies

The Institute of Cost Accountants of India

CMA Bhawan, 12, Sudder Street, Kolkata – 700 016

www.icmai.in

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Preface

Professional education systems around the world are experiencing great change brought about by the global demand. Towards this end, we feel, it is our duty to make our students fully aware about their curriculum and to make them more efficient.

Although it might be easy to think of the habits as a set of behaviours that we want students to have so that we can get on with the curriculum that we need to cover. It becomes apparent that we need to provide specific opportunities for students to practice the habits. Habits are formed only through continuous practice. And to practice the habits, our curriculum, instruction, and assessments must provide generative, rich, and provocative opportunities for using them.

The main purpose of this volume is to disseminate knowledge and motivate our students to perform better. Thus, we are delighted to inform about the **e-distribution of the first edition of our 'Work book' for Foundation level.**

This book has been written to meet the needs of students as it offers the practising format that will appeal to the students to read smoothly. Each chapter includes unique features to aid in developing a deeper under-standing of the chapter contents for the readers. The unique features provide a consistent reading path throughout the book, making readers more efficient to reach their goal. Discussing each chapter with illustrations integrate the key components of the subjects.

It is our hope and expectation that this new edition of work book will provide further an effective learning experience to the students.

The Directorate of Studies,

The Institute of Cost Accountants of India

FUNDAMENTALS OF ECONOMICS AND MANAGEMENT

FOUNDATION

PAPER – 1

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Suggested Marks Distribution from Examination Point of View

Only for Practice Purpose

Total 100 Marks	3 Hours	MCQ = 60 Marks
		Others = 40 Marks

Objective Question

60 Marks (1 Mark each questions)	MCQ
	True/False
	Matching

Short Notes

Minimum Marks for each Questions	4 Marks
Maximum Marks for each Questions	7 Marks

Practical Problem

Minimum Marks for each Questions	6 Marks
Maximum Marks for each Questions	8 Marks

SECTION – A : ECONOMICS
Study Note – 1
Basic Concepts of Economics

Learning Objective:

There is no end of people wants. When one or two wants is satisfied, more new wants are felt successively. But the means or resources are limited. People do not get sufficient resources which are needed to satisfy the unlimited wants. So the resources are always scarce in relation to the wants of the individuals, state or the government. Under this situation we have to choose the more urgent wants. Economics is an idea which makes a relationship between scarce means and unlimited wants.

I. Choose the correct answer

1. Who was the father of Economics

(a) Marshall

(b) Adam smith

(c) Robbins

(d) Keynes

2. Normative Economic theory deals with .....

(a) What to produce

(b) How to produce

(c) Whom to produce

(d) How the problem should be solved

3. Cetrisperibus means

(a) Demand constant

(b) supply constant

(c) Other thing being constant

(d) none

4. Micro Economics theory deals with.
   (a) Economy as a whole
   (b) Individual units
   (c) E conomic growth
   (d) all the above

5. In economics goods includes material things which …
   (a) A can be transferred
   (b) can be visible
   (c) both A & B
   (d) None

6. Human wants are
   (a) limited
   (b) unlimited
   (c) undefined
   (d) none

7. Nature of PPF curve is ….
   (a) convex to the origin
   (b) concave to the origin
   (c) both
   (d) none

8. If PPF is linear it implies …
   (a) constant opportunity cost
   (b) diminishing apart cost
   (c) Increasing opportunity cost
   (d) none

9. Any point beyond PPF is ….
   (a) attainable
   (b) unattainable
   (c) both
   (d) none

10. If an economy is working at the point left to PPF curve that shows…
   (a) Full employment
   (b) unemployment
   (c) excess production
   (d) none

Answer.

1. B
2. D
3. C
4. B
5. C
6. B
7. B
8. A
9. B

II. Fill in the blanks

1. **A ccording to _____ Economics is the study of science of wealth.**
2. **According to _____ definition economic is a social science.**
3. **A ccording to _____ top priority is given to man.**
4. **A ccording to _____ Robbins Economics must be ___ between ends.**
5. **A lternative uses of limited resources leads to _____**
6. **According to ____ definition Economics analytical science.**
7. **Growth definition is mostly associated with _____**
8. **____ definition includes welfare definition and scarcity definition.**
9. **In deductive method the logic proceed from ___ to ____.**
10. **In inductive method the logic proceed form ____ to ____.**

Answer.

1. J.B. Say
2. Welfare
3. Marshall
4. Neutral
5. Problem of choice
6. Scarcity
7. P.A. Samuelson
8. Growth
9. General to particular
10. Particular to general

III. State the statements true or False

1. **According to Adam Smith man is economic man ( )**
2. **According to Marshall Economic is normative science ( )**
3. **Positive science related with J.B. Say ( )**
4. **The terms micro & macro are introduced by Ragnar Frisch ( )**
5. **Science is practical, but Art is theoretical ( )**
6. **Positive science does not related to value judgments ( )**
7. **Gross investment = net investment + depreciation ( )**
8. **Consumption depends on not only present income but also future income ( )**
9. **Value paradox was depicted by law of demand ( )**
10. **PPC is also called PPF ( )**

Answer.

1. True
2. True
3. False
4. True
5. False
6. True
7. True
8. True
9. False
10. True

IV. Matching

1. Principles of economics	**A. Analytical method**
2. Wealth of nations	**B. Price theory**
3. An essay on the nature and significance of economic science	**C. Historical method**
4. Economic an introductory analysis	**D. Marshall**
5. Micro Economics	**E. MRT**
6. M acro Economics	**F. Production**
7. D eductive method	**G. Adam smith**
8. Inductive method	**H. P.A. Samuelson**
9. Opportunity Cost	**I. J.H. Keynes.**
10.Creation of utility	**J. Robbins**

Answer.

1. D
2. G
3. J
4. H
5. B
6. I
7. A
8. C
9. E
10. F

V. Short Answer type questions:

1. What is Economics?

Economics is a social science which studies the economic activities of human behavior like consumption, production, exchange etc. These studies basically explain "the human behavior as a relationship between given ends and scarce means which have alternative uses".

2. Define wealth.

The stock of goods under the ownership of a person 'or' a nation is called wealth. Wealth are of different types:

(a) Personal wealth:
The stock of goods under the ownership of a person is called personal wealth. For example: houses, buildings, furniture, land, money in cash, company shares, stocks of other commodities etc. Further, health, goodwill etc. can also be considered as a part of individual wealth. But in economics only transferable goods are considered as wealth.

(b) National Wealth:
The stock of goods under the ownership of a nation is called national wealth. It includes the wealth of all the citizens in the country. For example: natural resources, roads, parks, bridges, hospitals, public education institutions etc. If the citizen of the country holds a government bond it is personal wealth. But from the government point of view it is a liability. So, it should not be considered as the part of wealth of the nation.

3. Distinguish between wealth and welfare:

Welfare means well-being 'or' happiness. In general, if the wealth increases welfare also increases. However under following cases welfare might/ might not increase:

i. If a nation goes on creating wealth without paying any consideration to the health and mental peace of its citizens, it is doubtful whether the welfare increases or not.
ii. If the wealth is not distributed properly, it is also doubtful whether welfare increases or not.

4. What is money? Explain types of money prevailing in the economy.

Money is the most widely accepted medium of exchange. It is commonly used for exchanging goods or in settling debts. In ancient period, barter system was prevailed when some commodities were used as a medium of exchange by customs. It was called customary money. For example, use of cows in ancient India as a medium of exchange.

Constituents of Money Supply:

i. Rupee notes and coins

ii. Credit cards
iii. Traveler's cheque

5. Define Market. What are the functions of market?

In ordinary language, the term market refers to a place where the goods are bought and sold. But in Economics, it refers to a system by which the buyers and sellers establish contact with each other directly 'or' indirectly with a view to purchase and sell the commodity.

Functions of the Market:

a. To determine the price of the goods.
b. To determine the quantity of goods [supply]

Market Mechanism:

Market Mechanism means the totality of all markets i.e. the markets. The market mechanism determines the prices and quantities bought and sold of all the goods and services.

6. Define investment and mention its types.

An increasing the capital stock is called Investment.

Types of Investment:

(a) Real Investment:
An increase in the real capital stock is called real investment. For example machines, raw material, buildings and other types of capital goods.

(b) Portfolio Investment:
The purchasing of new shares of a company is called portfolio investment. It is noteworthy that **the** purchase of an existing share from another shareholder is not an investment. Because it cannot increase the capital stock of the company. It is the savings that are invested:

$Y = C + S$

(or)

$Y = C + I$

$S = I$

- Note: if there is foreign investment then $S \neq I$.

7. Distinguish between gross investment and net investment:

The Aggregate Investment made by an economy during a year is called gross investment. The gross investment includes

(a) Inventory Investment:
Investment in raw materials, semi finished goods and finished goods are called inventory investment.

(b) Fixed Investment:
Investment made in fixed assets like machines, building, factories shares etc. are called fixed investment.

Net Investment:

By deducting the depreciation cost of capital from gross investment the net investment can be obtained.

Net Investment = Gross Investment – Depreciation

8. Define Production. What are the factors of production?

Production refers to creation of goods for selling them into the market. In one word, production means 'Creation of utility". Suppose a child makes a doll for playing or for her enjoyment. It is not called production but the doll maker who sells these dolls in the market is engaged in production.

Factors of production:

The goods and services with the help to carry out the process of production are called factors of production. There are four factors of production viz.,

i) Land ii) Labour iii) Capital iv) Organization

The factors of production are also called inputs. The goods and services produced with the help of inputs are called output.

9. Define consumption. What are the determinants of consumption.

Consumption is defined as the satisfaction of human wants through the use of goods and services. Determinants of consumption are listed as follows:

i. Present Income
ii. Future income
iii. Wealth income

10. Define saving.

Saving is defined as income minus consumption. Whatever is left in the hands of an individual after meeting the consumption expenditure is called saving. Saving is generated out of current income and also out of past income.

11. Define income.

The net inflow of money (purchasing power) of a person over a certain period is called income.
For example: Daily income, weekly income, monthly income and yearly income.

12. Distinguish between wealth and income

A person ('or' a nation) consumes a part of income and saves the rest. These savings are accumulated in the form of wealth. Wealth is a stock owned at a point of time. Income is a flow, over a period of time.

13. Define the concept of consumer surplus.

This concept was introduced by Alfred Marshall. This concept is derived from the law of diminishing marginal utility. Consumer surplus is the difference between willing price and actual price.
C.S. = Willing Price – Actual Price
or
C.S = Demand Price – Market Price

Definition:

The excess of price which a consumer would be willing to pay for a thing rather than go without the thing and over what he actually does pay.

14. Describe demand forecasting.

The success of the business firm depends upon the successful demand foresting. Estimation of future demand for product at present is called demand forecasting.

Methods of Demand forecasting:

i. Expert opinion method
ii. Survey of buyers intensions
iii. Collective opinion method
iv. Controlled experiments
v. Statistical method

VI. Important Questions:

(1) Explain the subject matter of Economics.

In economics, a want is something that is desired. Want is the starting point of economic activity. Wants leads to efforts. An effort leads to satisfaction. In a nutshell "Wants-Efforts-Satisfaction" is the subject matter of economics. Therefore this subject matter of economics is divided into four parts.
Consumption (ii) Production (iii) Exchange (iv) Distribution

(i) Consumption: It is an act to use the goods or service to satisfy the wants. In economics, Consumption is typically defined as final purchased by an individual that are not investments of some sort. If someone buys a house to live in, that should be defined as consumption. However, if they buy a house to rent out that should be defined as an investment. Similarly, if they buy a car to

drive, that's consumption. But if a car is bought to use for a business, that could be construed as an investment. In short, the reason for the purchase determines whether something is viewed as on investment or as consumption.

(ii) Production: In economics, production involves the creation of goods and services by using resources. It is a process to change the raw materials into final/finished goods. It is nothing but creation of utility. To produce anything so many factors are essential. All these factors are classified into four categories. They are: (a) Land (b) Labour (c) Capital (d) Organization

(iii) Exchange: It means change of the goods from one person to another person. Earlier, goods were exchanged for goods. It is called "Barter system". To overcome the inconveniences in the barter system money was invented. Now the goods are exchanged for money. Price is essential for the exchange of goods for money.

(iv) Distribution: Distribution means sharing of the income among the factors of production. The total income which is generated by selling of these goods and services in the market must be distributed among the factors of production in the form of rent, wages, interest and profits.

There are two types of distribution

a. Micro distribution
b. Macro distribution

a. Micro Distribution

Micro distribution is nothing but pricing of factors of production. It means how the price (rent) per a unit of land is determined in the theory of rent (viz., Ricardian theory of rent, modern theory of rent etc.) . In the same way price determination per unit of labour, capital, and organisation are also discussed in different wage theories, interest theories and profit theories.

b. Macro Distribution

Macro distribution means sharing of the total national income among the total factors of production. In other words, we get to know whether the income is distributed properly or not properly among the people in the society.

Modern economists extended the subject matter of economics. to add some other concepts also like (a) Employment (b) Income (c) Planning and Economic development (d) International trade.

(2) How can you define economics?

The definitions of economics can be classified into four categories.

(a) Wealth definitions (b) Welfare definitions (c) Scarcity definitions (d) Growth definitions

Wealth definitions

Almost all classical economists followed wealth definition. It is mostly associated with J.B. Say and Adam smith. Adam smith was called "Father of economics". In his book "An enquiry into the nature and causes

of Wealth of nations (1776)" Adam Smith delinked the economics from political economy and he explained it in a scientific manner.

Definitions:

According to J. B. Say, "economics is the study of science of wealth.

According to Adam Smith, "economics is the science which deals with the wealth".

According to the above definitions:-

- Economics explains how the wealth is produced, consumed, exchanged and distributed.
- According to Adam Smith man is an economic man.
- Economics is a science of study of wealth only.
- This definition deals with the causes behind the creation of wealth.
- It only considers material wealth.

Criticism:

This definition was criticized by many philosophers like Carlyle, Ruskin, Walrus, and Dickens and others. According to the critics, economics is a decimal science, Gospel of Mammon, bread and butter science, uncompleted science etc. Further, wealth is of no use unless it satisfied human wants. This definition is not of much importance to man and his welfare.

Welfare definition:

This definition was given by Alfred Marshall. He was the follower of Adam smith. He wrote a famous book "Principles of Economics" in 1870.

Definition:

"Economics is the study of mankind in ordinary business of life. It examines that part of individual and social action which is most closely connected with the attainment and with the use of material requisites of well being".

According to Alfred Marshall's definition, economics is the study of wealth on the one hand and more importantly it is the study of human welfare on the other hand.

Main Points:

1. According to this definition, economics is a social science.
2. According to definition, goods are classified into two categories (a) material goods (b) immaterial goods.
3. According to Alfred Marshall, economics is a normal science.
4. The top priority is given the welfare of man while secondary priority is given to the wealth.
5. Marshall enhanced the status of man from economic man to social man. Economics related only some material goods that promote the human welfare.

Criticism:

This definition was criticized by Lionel Robbins on the following grounds:

1. According to Robbins, welfare definition is incomplete.
2. According to Robbins, economics must be neutral between ends.
3. Marshall neglected some materials goods that do not promote human welfare, but these goods
   are also produced, exchanged & consumed. So, they also come under the subject matter of economics.

Example: Cigarette and alcoholic products.

Scarcity Definition/Robbins definitions

This definition was given by Lionel Robbins. He wrote a famous book "an essay on the nature and significance of economic science" (1932).

Definitions:

"Economics is a science which studies human behavior as a relationship between ends and scarce means which have alternative uses". – ***Robbins***

Main Points:

According to the above definition,

i. Wants are unlimited
ii. Resources are limited.
iii. These resources have alternative uses.
iv. There are problem of choice of these resources.

Merits:

1. According to this definition, economics is an analytical science.
2. Economics turn into universal science.
3. According to Robbins, it is a positive science.
4. Economists are neutral between ends.

Criticism:

These definitions also criticized by so many economists on the following grounds:

1. It is not a universal science.
2. It is not applicable to developed countries.
3. Not applicable to communist (or) dictatorship countries.
4. It is not applicable to developing countries like India.
5. It also neglects the dynamic concepts.

Growth Definition

This Definition was given by J.M. Keynes and P.A. Samuelson in the book "Economics - An Introductory Analysis (1948)" written by Samuelson.

Definitions

Economics is the study of how men and society choose with 'or' without use of money to employ the scarce productive resources that would have alternative uses to produce various commodities overtime for distribution them for consumption now or in future among the various persons and groups in the society. It Analysis the costs and benefits of improving pattern or resource [use allocation]. - ***P.A. Samuelson***

Main points:

1. Like the scarcity definition it also accepts the unlimited wants and limited resource which have alternative uses.
2. According to Samuelson, the problem of scarcity of resources not only confined to present but also to the future. It means he introduced the concept of time element.
3. He also adopted a dynamic approach to the study of economics considering economic growth as an integral part of economics.
4. This definition includes Marshall's welfare definition and Robbin's scarcity definition.

(3) Explain the Scope of Economics

There are two approaches to explain the scope of economics: (i) Traditional approach (ii) Modern Approach

Traditional Approach

- Economics is a social science.
- It studies man's behaviour as a rational social being.
- It considered as a science of wealth in relation to human welfare.
- Earning and spending of income was considered to be end of all economic activities.
- Wealth was considered as a means to an end – the end being human welfare.

Modern Approach

- An individual, either as a consumer or as a producer, can optimize his goal and this is an economic decision.
- The scope of Economics lies in analyzing economic problems and suggesting policy measures.
- Social problems can be explained by abstract theoretical tools or by empirical methods.
- In classical discussion, Economics is a positive science.
- It seeks to explain what the problem is and how it tends to be solved.
- In modern time it is both a positive and a normative science.

- Economists of today deal economic issues not merely as they are but also as they should be.
- Welfare economics and growth economics are more normative than positive.

(4) Differentiate between microeconomics and macroeconomics.

The terms 'Micro' and 'Macro' are introduced by Ragnar Frisch in economics. According to him, the economics is studied in two ways viz., Micro level and Macro level.

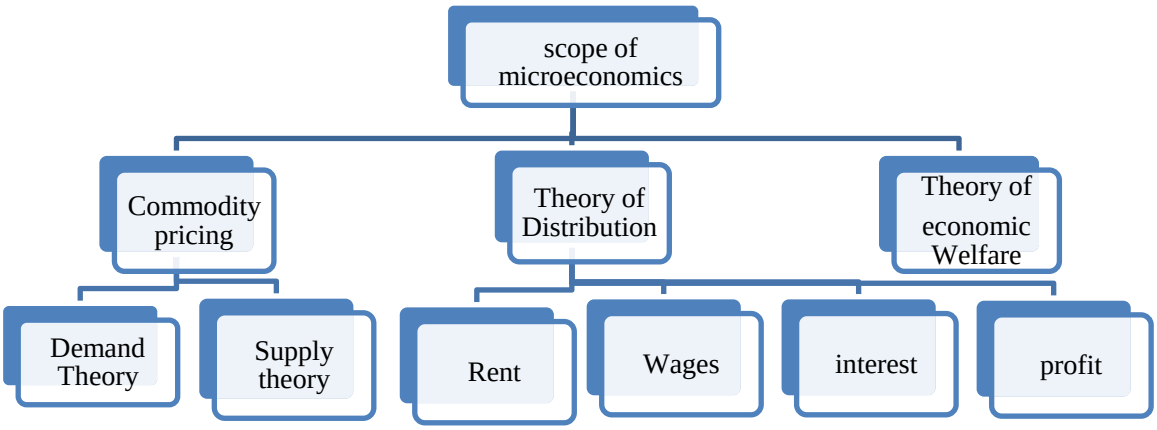
Meaning of microeconomics:

The word Micro is derived from Greek work 'Mikros', means very small or Millionth part. It studies about the behavior of Individual units. Individual units are a consumer, a producer, a firm or industry. Marshall

developed the microeconomics very well. According to Marshall, the microeconomics divide the economy into small units or small parts each part is studied. It explains how a consumer gets maximum satisfaction how the producer gets maximum output and how the firm gets maximum profits.

Definition:
Microeconomics is study of particular firm particular household, individual prices, wages, incomes,individual Industries, particular commodities". - ***K. E. Boulding***

Scope of microeconomics:
The microeconomics not only explains how the price of a good is determined and how the price per unit of factors of production is determined but it also deals with theories of economic welfare. So microeconomics is called "Price theory".



Uses or significance of microeconomics:

1. Understanding the operations of economy
2. Economic welfare of people.
3. Managerial economics

Macroeconomics

The word "Macro" is derived from Greek word "Makros", "large or very big". The Macro economics studies the economy as a single unit. It does not deal with Individual units. It deals with the aggregates 'or' totals and averages.

For example: national income, full employment, total output, total investment, total consumption etc.

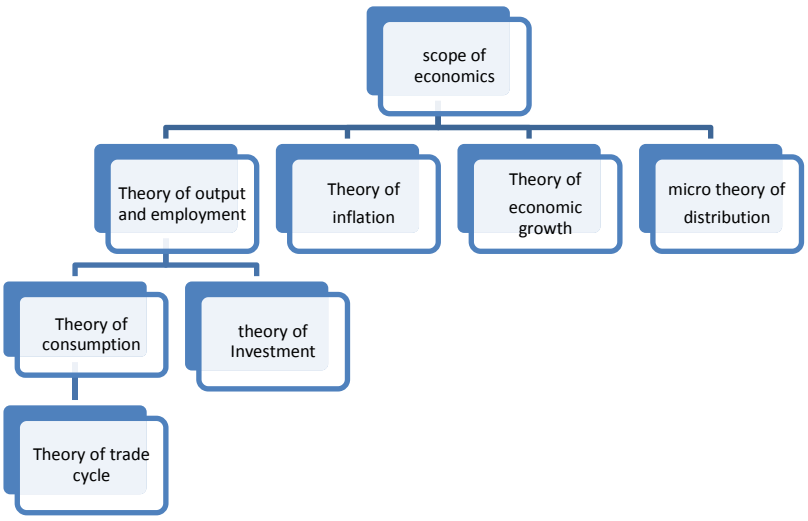
Definition:

According to Gardner Ackaly, "Macro economics is concerned with such variables as a aggregate volume of output of a economy with the extend to this resources are employed with the size of the national income and with the general price level.

Scope of macroeconomics:

Macro economics studies about the National Income i.e. calculation of the national income, trends in the national income etc., It also deals with total employment (full employment), total output etc.

It also studies about trade cycles, Inflation etc., It also deals with theories of economic growth and macro theory of distribution. It is also called Income and Employment theory.
Both Micro and macro economics are interdependent. From 1930 onwards there is an importance to the macroeconomics. Scope of macroeconomics can be explained by the following chart.



The macroeconomics analyses following problems of the economy:

i. Level of output and employment
ii. Fluctuation in level of output, employment and national income
iii. Changes in the general price level

iv. Economic growth and economic development
v. Theories of distribution

Significance of macroeconomics:

1. Understanding the working of an economy
2. Formulating policies
3. Preparing the economic plans
4. Take the remedial measures of trade cycles & Inflation

(5) Do you think that economics is science or arts? Explain in detail.

The term science implies:-

1. A systematic body of knowledge which traces the relationship between cause and effect.

2. Observation of certain facts, systematic collection and classification and analysis of facts.
3. Making generalization on the basis of relevant facts and formulating laws or theories thereby.
4. Subjecting in the theories to the test of real world observations.
5. Like the physics chemistry and botany economics also satisfy the above four characteristics.

Economics is regard as science.

Economics as an arts:

Keynes defines Arts as 'a system of rules for the attainment of a given end". The objective of Arts is to lay out rules to be used for the formulation of policies.

Difference between science and Arts:

i. Science is theoretical but arts is practical.
ii. A science teaches us "to know" while an arts teaches us "to do".
iii. Economics as a science in methodology and arts in its application.
iv. Economics is both science and arts.

(6) Whether economics is a positive science 'or' a normative science? Show your arguments.
Economics as a positive science:

1. The positive science explains "what it is" but not "what ought to be"
2. It explains about the things as they are
3. It does not deal with value judgments.
4. According to Lionel Robbins economics is a Positive science

Economics as a Normative Science:

1. A normative science explains what ought to be and what not ought to be.
2. It does relates to value judgments

3. It deals with good & bad (or) right and wrong.
4. According to Alfred Marshall economics is a normative science.
5. Economics is both positive and normative science.

(7) Distinguish between deductive method and inductive method

Deductive Method:

1. It is also called prior method, abstract method and analytical method.
2. In this method the laws or theories are prepared on the basis of fundamental assumptions.
3. In this method the logic proceeds from general to particulars.

For example: law of D.M.U, law of equi-marginal utility, law of consumer surplus etc.

4. Classical economists followed deductive method.

Inductive Method:

1. This method is also known as historical method 'or' statistical method.
2. In this method the laws 'or' theories are prepared on the basis of facts 'or' statistical data.
3. In this method the logic proceeds from particular to general.
   For example: law of variable proportions, law of returns to scale, population theories etc.
4. Modern economist followed Inductive method.

(8) Describe the central problem faced by all economies.

Due to the scarcity of resources every economy should face some problems. The central problems faced by all economies can be explained as follows:

What to produce

If the present is given importance, then resources are diverted for the production of consumer goods. If future is given importance then resources are diverted for the production of capital goods.

How to produce

This problem is arising because of unavailability of some resources. A country may produce by using labour intensive technique 'or' capital intensive technique, depending upon its man power and stock of capital.

For whom to produce

A country may produce mass consumption goods at a large (for poor people) 'or' goods for upper classes. It is depend upon policies of the government.

(9) State and explain the law of diminishing marginal utility in detail.

The law of D.M.U explains the common experience of every consumer. It is based upon one of the characteristics of wants i.e. "A particular want is suitable". According to this law when a person goes on increasing the consumption of any one commodity the additional utility derived from the additional unit goes on diminishing. So, it is called law of diminishing marginal utility. The law of D.M.U was firstly profounded by H.H. Gossan in 1854. Hence it is called Gossans' first law of consumption. The law of D.M.U was developed by Alfred Marshall.

Definition:

"The additional benefit which a person derives from a given increase in stock of anything diminishes with every increase in the stock that he already has". – ***Marshall***

Different concepts in this law:

1. **Total utility:**

It is the total amount of satisfaction obtained by the consumer by the consumption of total units of a thing. The sum of marginal utilities is also called total utility.

TUx = f[Qx]

Or

TUx = ΣMUx

2. **Marginal Utility:**

It is the additional utility obtained by the consumer by the consumption of additional unit of a thing 'or' one more unit of a thing. The change in the total utility is called marginal utility.

$MU_X = \frac{\Delta U}{\Delta X}$

Or

$MU_n = TU_n - TU_{n-1}$

Table explanation:

Units	Total utility	Marginal utility
1	0	0
2	40	70
3	90	20
4	100	10
5	100	0
6	90	-10

Main Points:

1. When total utility increases, the marginal utility diminishes. Therefore, T.U. Curve slopes upwards from left to right and M.U. curve slope downwards from left to right.
2. When the total utility reaches the maximum, the marginal utility is zero. At this point T.U. curve reaches the peak and M.U. curve intersects 'X' axis.
3. When the total utility goes on diminishing then the M.U becomes negative. Therefore, the T.U. curve slopes downwards and M.U curve crosses the x-axis.

Assumptions:

1. The units are Homogeneous.
2. The units must be reasonable size.
3. There is a onetime gap between one unit of consumption and other unit of consumption.
4. There is no changes in the taste and preferences of consumer.

Exceptions:

1. Collection of the rare goods.
2. Hobbies
3. Misers
4. Money and gold
5. Reading 'or' books

Importance:

1. Value paradox
2. Basis for economic laws
3. Finance Minister
4. Re-distribution of wealth

(10) Define Production Possibility Curve (PPC). What are its salient features?

The PPC is also called production possibility frontier, production possibility boundary and production transformation curve. The PPC curve shows the various combinations of two commodities that can be produced by an economy with the given resources and given technology. This is shown in figure 1.

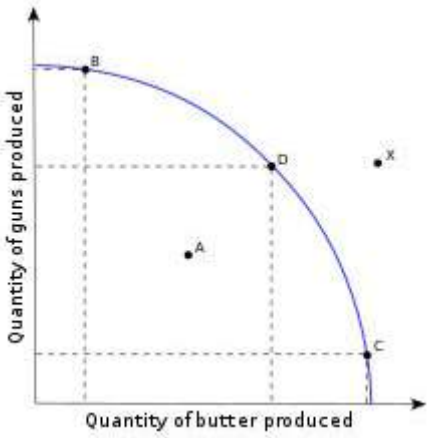


Figure: 1

Figure 1 shows the production possibility curve between two goods viz., guns and butter.

Main points:

i. The PPC curve always slopes downwards form left to right. Because when the production of one commodity is increases, the production of the other commodity decreases and vice versa.

ii. It is concave to the origin because MRT goes on increasing.

iii. The slope of the PPC at any given point is called marginal rate of transformation (MRT). The slope defines the rate at which production of one good can be redirected into production of other. It is also called opportunity cost.

Note:

- If the PPC curve is straight line, the opportunity cost is constant.
- All the combinations which lie on the PPC curve are possible combinations.
- The points beyond the PPC curve are impossible combinations.
- Shift of the PPC curve is nothing but economic growth.
- Any point that lies below the PPC curve is feasible combination. However, if the economy is
- working below the PPC curve that indicates the unused resources ‘or’ unemployment.

SECTION – A : ECONOMICS
Study Note – 2
Theory of Demand and Supply

Learning Objective:

In this Chapter, Theory of Demand and Supply are discussed. The Theory of Demand and Supply is a central concept in the understanding of the Economic system and its function. The quantity demanded of a good or service is the amount that consumers plan to buy during a particular time period, and at a particular price.

I. Choose the correct answer:

1. Point elasticity was propounded by
- **(a) Adam smith**
- **(b) Marshall**
- **(c) Robbins**
- **(d) Keynes**

2. Luxury goods have ____ degree of electricity
- **(a) High**
- **(b) low**
- **(c) Moderate**
- **(d) none**

3. The demand for salt is inelastic, because
- **(a) of low price**
- **(b) absence of it makes food tasteless**
- **(c) no substitutes**
- **(d) All the three**

4. Price electricity demand of product will be more elastic if it
- **(a) has no substitutes**
- **(b) has number of substitutes**
- **(c) is an item of necessity**
- **(d) is life saving product**

5. If price elasticity of demand is unity, the demand curve will be a
   (a) downward sloping curve
   (b) downward sloping straight line
   (c) downward sloping rectangular hyperbola
   (d) upward rising curve

6. If the price of burger rises for ₹ 12 per piece to ₹ 20 per piece as a result of which the daily sales decrease from 300 to 200 pieces per day. The price elasticity of demand can be estimated as
   (a) 0.5
   (b) 0.8
   (c) 0.25
   (d) 2.10

7. In case of substitute goods cross demand curve will be
   (a) downward sloping
   (b) upward rising
   (c) parallel to vertical axis
   (d) parallel to horizontal axis

8. An increase in price will result in an increase in total revenue if
   (a) percentage change in quantity demanded in greater than the percentage change in price
   (b) percentage change in quantity demanded is less than the percentage change in price
   (c) percentage change in quantity demanded is equal to the percentage change in price
   (d) none

9. When demand curve is perfectly elastic, it will be
   (a) parallel to vertical axis
   (b) rectangular hyperbola
   (c) parallel to horizontal axis
   (d) downward sloping linear

10. If the price elasticity of demand for wine is estimated to be -6, then a 20% increase in price of wine will lead to …….. in quantity demanded of wine at that price
   (a) 12% increase
   (b) 12% decrease
   (c) 19.6% increase
   (d) 20.6% decrease

11. Which of the following is not a factor in market supply of a product
   (a) cost of production
   (b) number of buyers
   (c) market price of the product
   (d) price of related products

12. Which of these will have highly inelastic supply

(a) perishable goods
(b) consumer durables goods
(c) Items of elite class consumption
(d) All the three

13. The supply function of a product x is as Sx = 5px+3. Where px stand for price. The quantity supplied corresponding to price of ₹ 2 will be ……

(a) 18
(b) 13
(c) 15
(d) 23

14. An improvement in technology will cause supply curve

(a) shift rightward
(b) shift leftward
(c) remain unchanged
(d) shift rightward and leftward

15. When there is an excess demand in the market, equilibrium price will

(a) fall
(b) rise
(c) remain unchanged
(d) initially fall then rise

Answer.

1. (b)
2. (a)
3. (c)
4. (b)
5. (a)
6. (b)
7. (a)
8. (b)
9. (a)
10. (b)
11. (d)
12. (a)
13 (b)
14 (a)
15 (b)

II. Fill in the blanks

1. **According to law of demand, there is a _____ relationship between price and demand.**
2. **If two or more than two goods are used to satisfy the same want are called _____.**
3. **In case of inferior goods, if the income rises than the demand _____.**
4. **Increase in demand due to the change in other things is called _____ in demand curve.**
5. **Total outlay method is also called _____.**
6. **Monopoly fixes the fewer prices if the demand is _____ elastic.**
7. **If there is no possibility to postpone the consumption of the commodity than the elasticity is _____.**
8. **Supply curve in the case of labour is _____.**
9. **If the supply curve is parallel to ox-axis than the supply is _____**
10. **Perfectly elastic demand curve is _____**
11. **In case of land supply curve is _____**
12. **If input prices rise supply curve shifts to the _____**
13. **For a giffen good, demand curve will be _____**
14. **If demand for a commodity is elastic, total revenue will _____ , as price decreases.**
15. **If supply increases more than demand, equilibrium price will _____**

Answer

1. Inverse
2. Complementary goods
3. Decreases
4. Shift
5. Total expenditure
6. more
7. less
8. Backward bending
9. Unlimited
10. parallel to ox-axis
11. Perfectly Inelastic
12. Left
13. Upward sloping
14. Rise
15. Fall

III. State the sentence true or false

1. **In ordinary language demand means desire ( )**
2. **There is a inverse relationship between income and demand ( )**
3. **Consumers tastes can influence the demand ( )**
4. **Change in the demand due to the change in price is called extension of demand ( )**
5. **In case of exception of law of demand of the price demand curve slopes downwards from left to right ( )**
6. **Comfort goods have more elastic demand ( )**
7. **Price discrimination is possible due to elasticity ( )**
8. **The supply curve in case of land is parallel to x-axis ( )**
9. **If there is more increase in demand and less income in supply, then quantity and price rises ( )**
10. **If there is more decrease in supply and less decrease in demand then quantity decrease and price rises ( )**
11. **For necessary goods demand will be relatively more elastic ()**
12. **When government imposes tax on a commodity its supply will shift to the right ().**
13. **If the cross price elasticity of demand for two goods is positive, goods are called substitutes ()**
14. **For a linear demand curve, point elasticity at the midpoint is greater than one ()**
15. **Supply curve of labour is upward sloping ()**

Answer

1. (T)
2. (F)
3. (T)
4. (T)
5. (F)
6. (F)
7. (T)
8. (F)
9. (T)
10. (T)
11. (F)
12. (F)
13. (T)
14. (F)
15. (F)

IV. Match the following

A	B
1. law of demand	A .income demand
2. substitution effect	B. movement on DD curve
3. superior goods	C . Prime factor
4. Contraction of demand	D . inelastic demand
5. Decrease in demand	E . demand curve
6. Durable goods	F . elasticity of demand
7. Unitary elastic DD curve	G . Rectangular hyperbola
8. Business decision	H. government policy
9. Supply	I . M arshall
10. Electricity of supply	J. shift of DD curve
11. Complementary goods	K. Unitary elastic demand
12. Luxury goods	L. downward sloping cross demand
13. Imposition of subsidies	M. Rise in equilibrium price
14. Excess demand	N. Rightward shift of supply
15.Comfort Goods	O. Relatively Elastic Demand curve

Answer

1. (I)
2. (E)
3. (A)
4. (B)
5. (J)
6. (D)
7. (G)
8. (F)
9. (H)
10. (C)
11. (L)
12. (O)
13. (N)
14. (M)
15. (K)

V. Answer following questions:

1. Define Law of Demand. Distinguish between individual demand and market demand.

Meaning of Demand

Demand means 'desire. However, in economics demand means desire backed by the purchasing power and willing to pay the price.

Law of Demand:

It explains the functional relationship between price and quantity demanded. According to law of demand when all other things remain constant, if the price rises demand is decreased. If the price falls demand will be increased. It means there is an inverse relationship between price and demand.

Dx = f [Px]

Demand Schedule:

It shows the various quantities of the goods that are demanded at various levels of prices. There are two types of demand schedules: 1. Individual Demand Schedule 2. Market Demand Schedule

a. Individual Demand Schedule:

It shows the various quantities of goods that are demanded by an individual at various levels of prices in the market. It can be shown by table 1

Table 1

Price	Demand
150	20
100	25
50	30

From this demand schedule, we can derive demand curve as shown in figure 1.

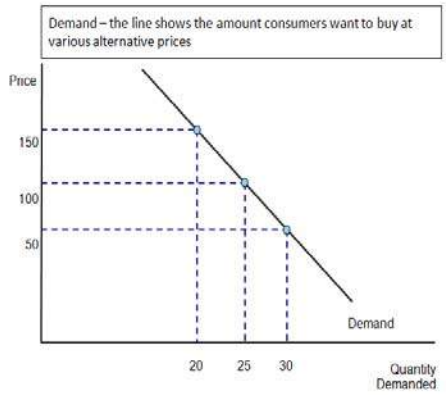


Figure: 1

Figure 1 shows negative relationship between quantity demanded and corresponding price that is represented by a downward sloping straight line.

Derivation of market demand from individual demand

b. Market Demand Schedule:

It shows the various quantities of the goods that are demand by all the consumers in the market at various levels of prices in the market. When the individual demands are added market demand can be obtained

Table 2

Price	Demand		
	Consumer 1	Consumer 2	Market Demand (1+2)
15	4	2	6
10	5	8	13

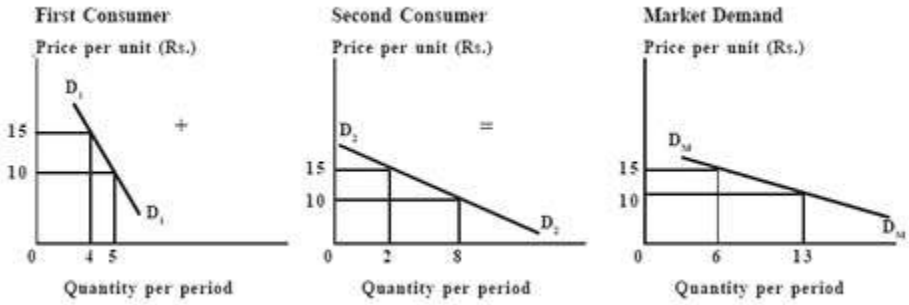


Figure: 2

Market demand schedule is graphically represented by market demand curve (Figure 2) which is the horizontal sum of individual demand curve. Market demand curve is always downward sloping.

2. Why demand curve is downward sloping? Mention exceptions to the law of demand

There are many reasons for the falling nature of demand curve. Some of the reasons are explained as follows:

i. Law of diminishing marginal utility:

According to law of diminishing marginal utility when the quantity of goods is more the marginal utility of the commodity will be less. So the consumer demands more goods when the price is less. That is why, the demand curve slopes downwards from left to right.

ii. Substitution effect:

In the case of substitutes if the price of commodity 'x' rises relatively to the other good 'y' the consumer will buy less of commodity 'x' and buy more of the good 'y' which has become relatively cheaper. This is called substitution effect. So the demand curve slopes downward.

iii. Income effect:

The income effect tells that the real income of the consumer rises due to the fall in the price level. So they purchase more and more goods when the price falls. This is said to be the income effect.

iv. New buyers:

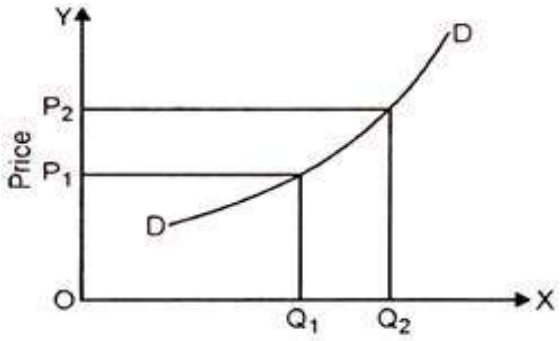
When the price of a commodity decreases the new consumers are attracted to that commodity because when the price level falls it becomes cheaper good than before. So the demand will rise with the price falls.

v. Old buyers:

When the price of anything decreases the old buyers purchase more goods than before. So the demand will be increased. That is why, the demand curve slopes downward from left to right.

Exceptions of the Law of Demand:

The law of demand is a general statement stating that price and quantity demanded of a commodity are inversely related. But in certain situations, more will be demanded at a higher price and less will be demanded at a lower price. In such cases, the demand curve slopes upward from left to right which is called an exceptional demand curve as shown in the following diagram.



Quantity Demanded
[Exceptional Demand Curve]

Figure: 3

When price increases from OP_1 to OP_2, quantity demanded also increases from OQ_1 to OQ_2. This is contrary to the Law of Demand. The following are the exceptions to the Law of Demand.

i. Giffen Paradox (Necessary goods):

In the case of necessary goods the law of demand cannot be operated. This is observed by British economist, the Sir Robert Giffen. He observed in London the low paid workers purchases more of bread when its price rises. That's why, this situation is known as Giffen Paradox.

ii. Speculation:

Some times the price of a commodity might be increasing and it is expected to increase still further. The consumers will buy more of the commodity at the higher price than they did at the lower price. It is contrary to law of demand.

iii. Conspicuous:

These are certain goods which are purchases to project the status and prestige of the consumer e.g., expensive cars, diamond jewellery, etc. Such goods will be purchased more at a higher price and less at a lower price.

iv. Shares or Speculative market:

It is found that people buy shares of a company whose price is rinsing on the anticipation that the price will rise further. On the other hand, they buy less shares in case the prices are falling as they a expect a further fall in price of such shares. Here the law of demand fails to apply.

v. Bandwagon effect:

Here the consumer demand of a commodity is affected by the taste and preference of the social class to which he belongs to. If playing golf is fashionable among corporate executive, then as the price of golf accessories rises, the businessman may increase the demand for such goods to project his position in the society.

vi. Illusion:

Sometimes, consumers develop a false idea that high priced goods will have a better quality instead of a low priced good. If the price of such a good falls, they feel that its quality also deteriorates and they do not buy, which is contrary to the law of demand

3. Define Demand Function. What are the determinants of Demand ?

The demand function explains the functional relationship between demand for a commodity and determinants of the demands. This can be explained by the following equation.

Dn = f (Pn, Psc, Y , T…..)

Dn = Demand for commodity 'n'

f = functional relationship

Pn = Price of commodity 'n'

Psc = Prices of substitute and complementary goods.

Y = Income of the consumer.

T = Tastes and preference of the consumer.

Determinants of demand:

The demand for any commodity is depend upon so many factors. These factors are called determinants of demand. They are:

i. Price of the goods:

The demand for any commodity firstly depends upon its price. When the price rises demand decreases, when the prices falls demand increases.

ii. Prices of the substitute goods:

The demand for any commodity not only depends upon its price but also the prices of its substitute goods. For example, tea and coffee. Here the demand for tea depends upon price of the coffee.

iii. Prices of the complementary goods:

The demand for a commodity also depends upon the price of its complementary goods. For example, car and petrol. Here demand for petrol depends upon price of the car.

iv. Income of the consumer:

The income of the consumer also influences the demand for a commodity. When the income risespeople purchase the more quantity of goods. When the income falls they purchase less quantity of goods.

v. Tastes and preferences of the consumer:

The tastes and preference of the consumer can also determine the demand for a commodity. When the tastes are changed, the demand for goods also changed.

vi. Population:

When the population is increased, the demand for goods also increases. When the population decreases demand also decreases.

vii. Climate:

The climatic conditions also can influence the demand. In hot climatic conditions cool drinks are demanded. In rainy season umbrellas are demanded.

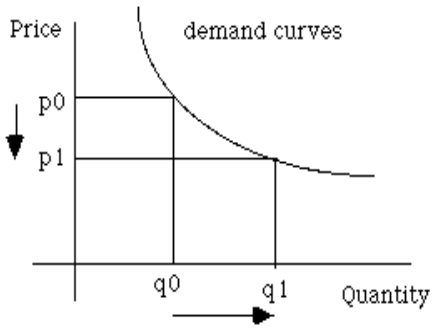
Types of Demand:

There are three types of demands. They are:

a. P rice demand
b. Income demand
c. Cross demand

a. Price Demand:

Price demand explains the relationship between price of a commodity and demand for that commodity. There is an inverse relationship between price and demand. So, the price demand curve slopes downwards from left to right : Dx = f [Px]



b. Income Demand:

Income demand explains the functional relationship between income of consumer and demand for goods. Generally if the level of income rises the consumer purchases more of goods. If the level of income decreases he purchases less quantity goods. It means there is a direct proportional relationship between income of consumer and demand of goods. So, normally the income demand curve slopes upwards form left to right. Dx = f [y]

The income demand curve is in two types:

In case of superior goods 'or' normal goods the income demand curve [I.D.] slopes upwards from left to right. Superior goods mean 'best quality goods'.

In the case of Inferior goods the I.D. slopes downwards form left to right inferior goods means "less quality goods.

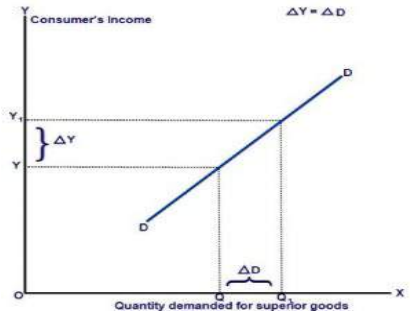


Figure: 4

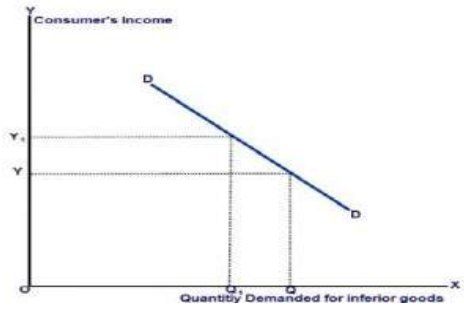


Figure: 5

Figure 4 represents the income demand function for normal/superior goods while figure 5 represents that for an inferior good.

c. Cross Demand:

It shows the relationship between price of one commodity and demand for another commodity. It means the demand for one commodity not only depend upon its price but also prices of its substitute goods and complementary goods: Dx = f [Py]

The cross demand curve is in two types:

It is upwards from left to right in the case of substitute goods and its slope downwards form left to right in the case of complementary goods.

Substitute goods:

If one good is used in the place of other good to satisfy the same want they are called substitute goods. **Example:** Tea & coffee, pen & pencil etc. In the case of substitute goods there is a direct proportion relationship between price of one commodity and demand for another commodity. Therefore, the crossed demand curve [CD] In this case upward from left to right.

Complementary goods:

If two 'or' more goods are used to satisfy the single want they are called complementary goods. **Example:** Milk, sugar, tea powder etc., are complementary for tea, cement, bricks, iron etc., are complementary for construction work. In this case of complementary there is inverse relationship between price of one commodity and demand for another commodity. Therefore, C.D In this case slopes downwards from left to right.

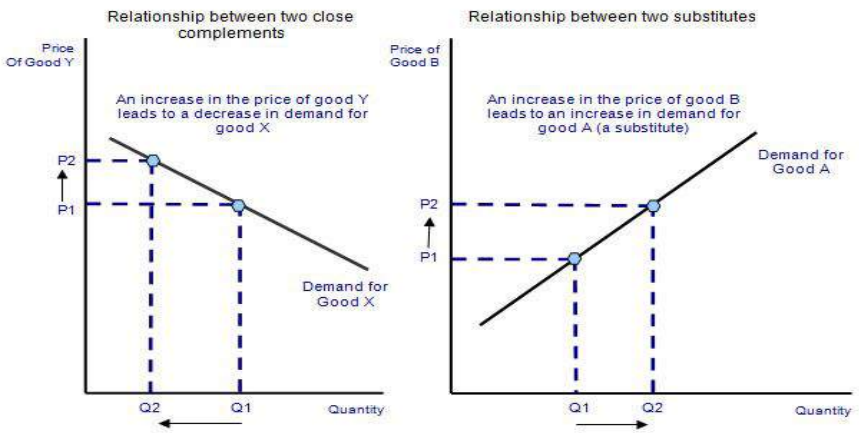


Figure: 6

4. Distinguish between change in demand and Change in quantity demanded.

If there is a change in the determinants of a demand that leads to the change in demand. These changes in demand are of two types. They are i. Extension and contraction of demand ii. Increase and decrease of demand.

i. Extension and Contraction of Demand:

When all other things remain constant if there is a change in the price that leads to the change in demand. These changes in demand are called extension and contraction of demand. When the price is decreased the demand is extended when the price is increased the demand is contracted. To explain the extension and contraction of demand a single demand curve is enough.

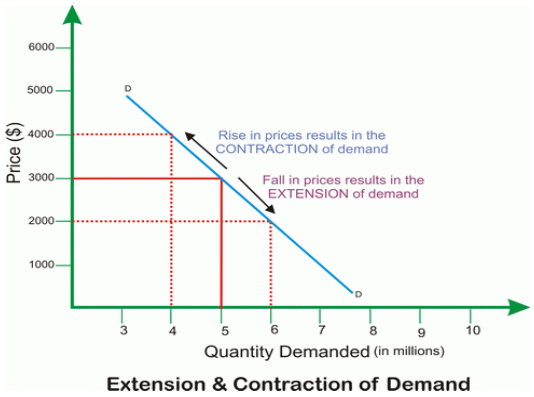


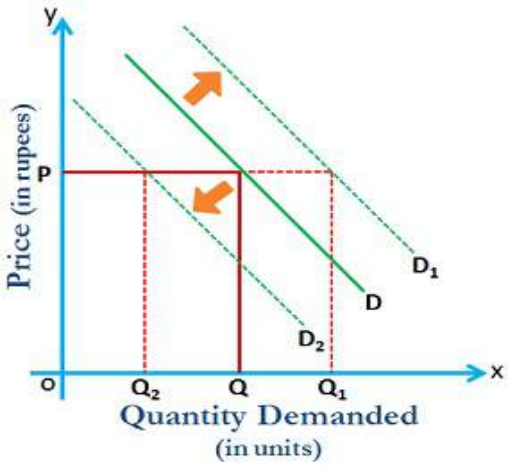
Figure: 7

ii. Increase and decrease of demand

When the price is constant, if there is a change in the other determinants that lends to change in demand. These changes in demand are called "Increase and decrease of demand". To explain the increase and decrease of demand single demand curve is not enough. It means new demand curves are formed.

a. When the demand is increased, the new demand curve is formed towards right to old demand curve 'or' preceding demand curve.

b. In the same way when the demand is decreased the new demand curve is formed towards left to old demand curve 'or' preceding demand curve.



5. Define elasticity of Demand. Mention types of elasticities of demand.

Meaning of Elasticity of demand

Elasticity means sensitiveness 'or' responsiveness. Elasticity of Demand means response in demand. The elasticity of demand explains change in demand due to the change in the determinants of the demand.

Type of Elasticity of demand

There are three types of elasticity of demand. They are:

I. Price elasticity of demand.
II. Income elasticity of demand
III. Cross elasticity of demand.

I. Price Elasticity of Demand:

It shows the relationship between proportionate change in the demand and proportionate change in the price. It means it explains how much change in the price and it leads to how much change in the demand.

E_p= Proportionate change in demand/ Proportionate change in Price

$$= \frac{\frac{dq}{q}}{\frac{dp}{p}} = \frac{dq}{dp} \times \frac{p}{q}$$

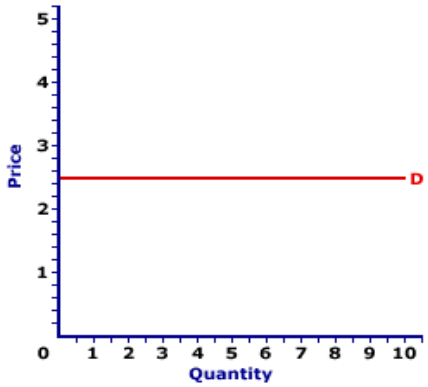
Types of price elasticity of demand:

There are five types of price elasticity of demand

1. Perfectly elastic demand (Ep= ∞)
2. Perfectly Inelastic demand (Ep = 0)
3. Relatively elastic demand (EP > 1)
4. Relatively Inelastic demand (EP< 1)
5. Unitary elastic demand (E_P = 0)

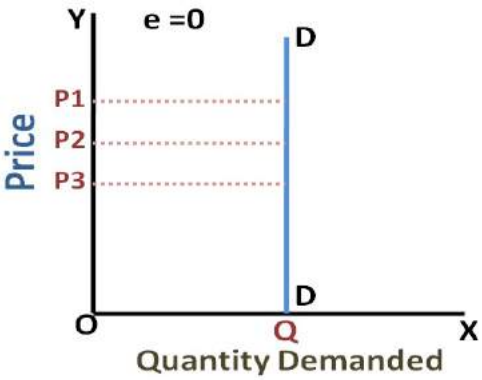
1. Perfectly elastic demand (E_P= ∞)**:**

When the price is constant if there is a change in demand it is said to be perfectly elastic demand. It means the demand may be increase 'or' decrease without change in price. Here the value of E_P is infinity. The demand curve in this case parallel to X axis.



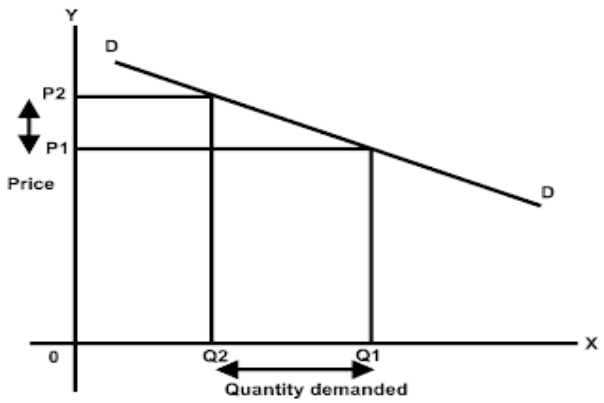
2. Perfectly Inelastic demand (E_P = 0)**:**

When the price is changed if there is no change in the demand it is said to be perfectly inelastic demand. It means the price may be increase 'or' decrease but the demand is constant Here the value of E_P = 0.The demand curve in this case parallel to Y axis.



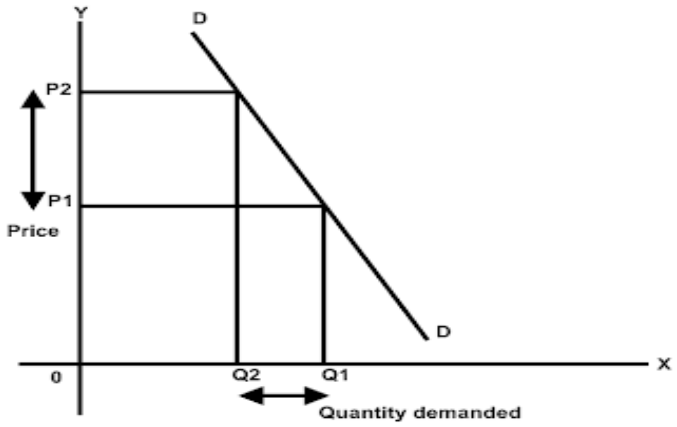
3. Relatively elastic demand (ex: luxury goods):

If the proportionate change in demand is more than proportionate change in the price. It is said to be relatively elastic demand. It means a little change in the price leads to more change in demand. Here the value of EP is greater than one the demand curve in the case slopes downward from left to right.



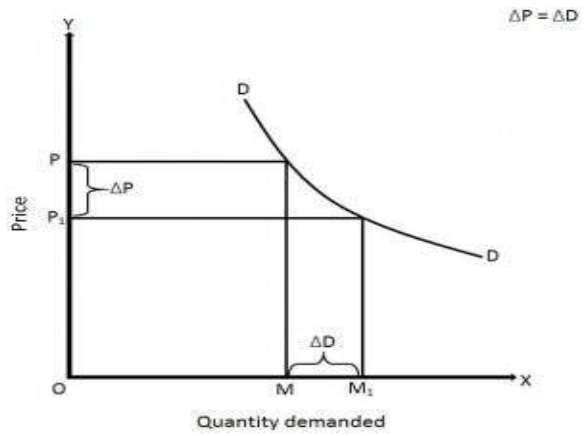
4. Relatively Inelastic demand (ex: necessary goods)

If the proportionate change in demand is less than proportionate change in the price. It is said to be relatively inelastic demand. It means a more change in the price leads to less change in demand. Here the value of EP is less than one. The demand curve in this case slopes down wards from left to right. But it is steeper than relatively elastic demand.



5. Unitary elastic demand:

If the proportionate change in the demand is equal to the proportionate change in the price. It is said to be unitary elastic demand. It means the change in the demand and change in price are same. Here the value of E_P is 1. Generally comfort goods have unitary elastic demand unitary elastic demand curve also slopes downwards from left to right but it is rectangular Hyperbola.



II. Income elasticity of demand:

It shows the proportionate change in demand and proportionate change in income. It means it explains how much change in the income and it leads to how much change in demand

E_Y = Proportionate change in demand / Proportionate change in income

$$E_Y = \frac{\frac{dq}{q}}{\frac{dY}{Y}} = \frac{dq}{dY} \times \frac{Y}{q}$$

Types:

- Perfectly elastic Income demand ($E_Y = \infty$)
- Perfectly Inelastic Income demand ($E_Y = 0$)
- Relatively elastic Income demand ($E_Y > 1$)
- Relatively Inelastic Income demand ($E_Y < 1$)
- Unitary elastic Income demand ($E_Y = 1$)

A. Perfectly elastic Income Demand

When the income is constant if there is a change in the demand. It is said to be perfectly elastic income demand. It means the demand may be increase 'or' decrease without change in income. Here the value of E_Y is infinity. The demand curve in this case parallel to X- axis.

B. Perfectly Inelastic Income demand:

When the income is changed if there is no change in the demand it is said to be perfectly inelastic income demand. It means the income may be increase 'or' decrease but the demand is constant Here the value of E_Y is zero. The demand curve in this case parallel to Y – axis.

C. Relatively elastic Income Demand:

If the proportionate change in the demand is more than proportionate change in income. It is said to be relatively elastic income demand. It means a little change in the income leads to more change in demand. Here the value of E_Y is greater than one. The demand curve in this case slopes downwards from left to right.

D. Relatively Inelastic Income Demand:

If the proportionate change in the demand is less than proportionate change in income. It is said to be relatively inelastic income demand. It means a more change in the income leads to less change in demand. Here the value of E_Y is less than one. The demand curve in this case slopes upwards from left to right.

E. Unitary elastic income demand:

If the proportionate change in the demand is equal to proportionate change in Income. It is said to be unitary elastic income demand. It means the change in the income and changes in the demand are same. Here the value of E_Y is one. The demand curve in this case also upward from left to right.

III. Cross elasticity of demand:

It shows proportionate change in the demand for one commodity and proportionate change in the price of other commodity. It means it explains how much change in the price of one commodity and it leads to how much change in the demand for another commodity

E_C= Proportionate change in demand for good X/ Proportionate change in price of good Y

$$\frac{\frac{dq_X}{q_X}}{\frac{dp_Y}{p_Y}} = \frac{dq_X}{dp_Y} \times \frac{p_Y}{q_X}$$

6. Mention the methods of measurement of price elasticities of demand.

There are four methods to measure the elasticity of demand. They are:

a. Percentage method

b. Total outlay method

c. Point method

d. Arc method

a. Percentage Method:

In this method to measure the elasticity of demand firstly we should find out the change in demand and change in price in percentages. Then the following formula can be used.

E_p= Proportionate change in demand /Proportionate change in Price

b. Total outlay Method:

In this method, based on the relationship between price and total expenditure, elasticity can be decided. If the total expenditure increases with the falling of the price and decrease with the raising of the price. It is said to be relatively elastic demand ($E_P > 1$).

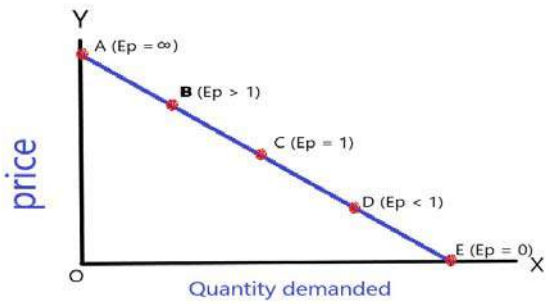
If the total expenditure is constant even the price increase 'or' decrease it is said to be unitary elastic ($E_P = 1$). If the total expenditure decreases with the falling of the price and increase with the raising of the price. It is said to be relatively in elastic demand ($E_P < 1$).

c. Point Method:

In this method the elasticity of demand can be measured at a particular point on the demand curve. In this method the following formula can be used.

E_p = lower segment / upper segment

Let we assume that AE is the demand curve in the diagram. Now the measurement of elasticity of demand along the demand curve AE is explained in the following way.



d. Arc Method:

If there are small changes in demand and prices, it is not possible to measure the elasticity of demand by the point method So, the Arc method is introduced. In this method, the following formula can be used : $E_p = \frac{\text{change in demand}}{\text{1st demand} + \text{2nd demand}} \div \frac{\text{change in price}}{\text{1st demand} + \text{2nd demand}}$

$$= \frac{q_2 - q_1}{q_1 + q_2} \div \frac{p_2 - p_1}{p_1 + p_2}$$

7. Explain the importance of elasticity of demand. What are its determinants?

Importance of Elasticity of Demand

The concept of elasticity of demand is of great practical importance in the sphere of government finance as well as in trade and commerce.

(i) Business Decision:

If the product has more elastic demand the business man fixes the less price, if the good has less elastic demand he will fix the more price.

(ii) Monopolist:

The monopolist fixes the more price in one market in which the elasticity of demand is less. And less price in more elastic demand market for the same thing (or) same good.

(iii) Determination of factor price:

The concept of elasticity of demand also helps in determining the price of various factors of production. Factor having in elastic demand gets higher price and factors having elastic demand gets lower price.

(iv) Route for international trade:

If demand for exports of a country in inelastic, that country will enjoy a favorable terms of trade while if the exports are more elastic than imports, then the country will lose in the terms of trade.

(v) To the government:

The concept of elasticity of demand also enable the government to decide as to what particular industries should be declared as 'public utilities' to be taken over and operated by the state.

Determinants of Elasticity of Demand:

(i) Nature of the commodity
(ii) Availability of substitutes
(iii) Variety of uses
(iv) Possibility of postponement of consumption
(v) Durable goods

(i) Nature of the commodity:

In the case of necessaries the demand is less elastic (or) comparatively inelastic. For example rice, salt, pulses, matchbox etc. On the other hand the elasticity of demand for luxuries is more elastic. For example, TV, DVD players, Gold, Diamonds etc. Comfort goods have unitary elastic demand.

(ii) Availability of substitutes:

If a commodity has substitute goods, the elasticity for that commodity is more elastic. For example, Lux soap, pears soap, ponds and Lakme creams.

(iii) Variety uses:

If the goods have several uses, the elasticity of demand for it is more elastic. For example, milk, coal, electricity etc.

(iv) Possibility of Postponement of consumption:

There are certain goods which can be postponed for purchase. In case of these goods, the demand is elastic. However, in the case of life saving medicines the demand will be inelastic because we cannot postpone the purchase of such goods.

(v) Durable goods:

In case of durable goods the elasticity of demand will be less, but in case of perishable goods the elasticity of demand will be more.

8. State the law of supply. How can you derive market supply curve from individual supply curve?

Supply means sum of the part of stock of the goods which is prepared by a seller to sell at a particular price, at a particular market in a particular period of time. The Law of supply explains the functional relationship between price of a good and supply of the good. When all other things remain constant, if the price rises supply also increase, if the price falls supply will be decrease. It means there is direct proportional relationship between price and supply.

Supply Schedule

It shows the various quantities of the goods that are supplied at various levels of prices. There are two types of supply schedule. They are

I. Individual supply schedule

II. M arket Supply schedule

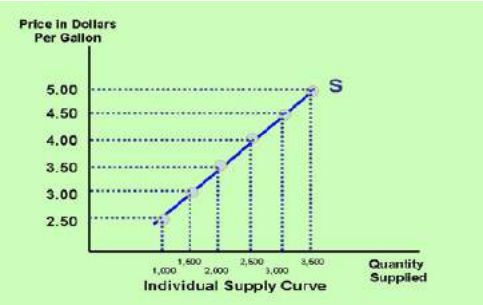
I. Individual supply schedule

It shows various quantities of the goods that are supplied by an individual seller (or) producer at various levels of prices in the market.It is shown in table 3

Table 3

Price (dollar/Gallon)	Supply
2.5	1000
3	1500
3.5	2000
4	2500
4.5	3000
5	3500

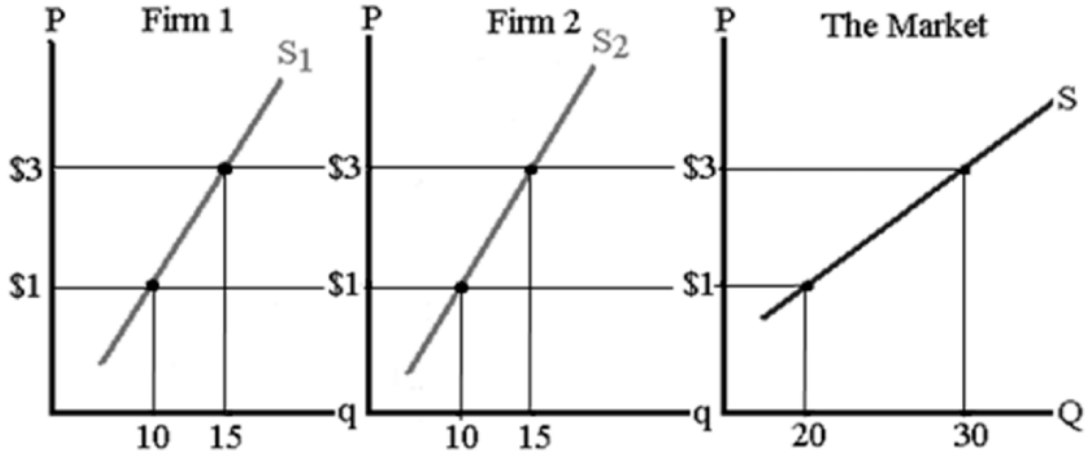
This individual supply schedule can be represented in terms of the following figure which is called indivual supply curve.



Since there is a positive relationship between price and quantity supplied, individual supply curve will be a positively sloped line.

II. Market Supply schedule:

It shows the various quantities of the goods that are supplied by various producers (or) sellers at various levels of prices in the market. When we add the supply of all sellers then total supply 'or' market supply can be obtained. Both the individual supply curve and market supply curve slopes upward from left to right as there is a direct proportional relationship between price and supply.



9. Distinguish between change in supply and change in quantity supplied. What are the exceptions to the law of supply?

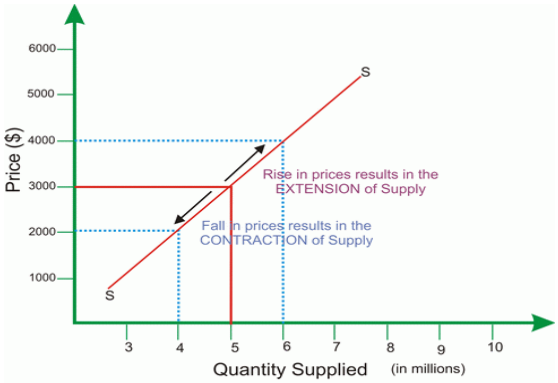
Change in Supply:

If there is a change in the determinants of the supply that leads to the change in supply. These changes in supply are two types. They are:

i. Extension and contraction of the supply
ii. Increase and decrease of the supply.

i. Extension and contraction of the supply:

When all other things remain constant if there is a change in the price that leads to change in the supply. These changes in the supply are called extension and contraction of the supply. When the price is increased the supply will be extended, when the price is decreased the supply will be contracted. The following diagram explains the extension and contraction of the supply.

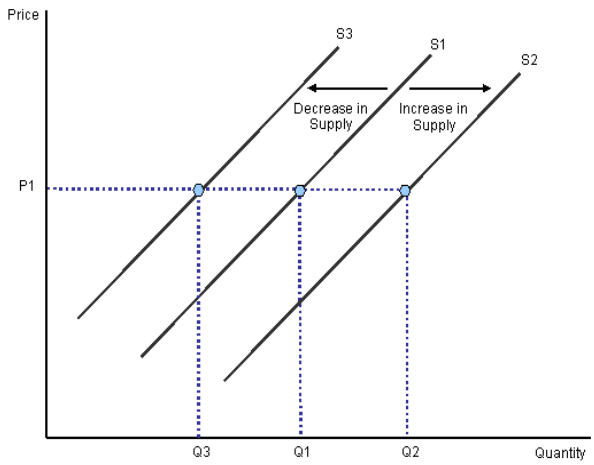


Extension & Contraction of Supply

ii. Increase and decrease of supply:

When the price is constant if there is a change in any one of the determinants that leads to change in supply. These changes in supply are called increase and decrease of supply. To explain the increase and decrease of the supply a single supply curve is not enough. It means new supply curves are formed.

- When the supply is increased the new supply curve is formed towards right to the old supply curve.
- In the same way when the supply is decreased the new supply curve is formed towards left to the old supply curve.



Exceptions to the law of supply:

- **Land (or) Agriculture goods**
  Land (or) Agriculture goods are limited in supply. Therefore, in the case of land (or) Agriculture goods the supply curve is parallel to Y-axis.

- **Rare goods.**
  In the case of rare goods supply cannot be changed according the price. So in the case of rare goods the supply curve is parallel to Y-axis.

- **Supply of labour.**

I n the case of labour, the supply curve is backward bending. Because in the initial stage if the wage level is increased the supply of the labour also increased. Beyond a certain stage if the wages are increased they require the more leisure. So, the supply of labour will be decreased.

10. Define supply functions. What are the determinants of supply.

Supply function:

The supply function explains the relationship between the supply and the factors that determines the supply. This can be explained through an equation: Sx = f (Px, PI, T, W, GP)

In the above equation

Sx = supply of goods 'x'

f = functional relationship

Px = Price of 'x'

Pl= Price of inputs (factors)

T = Technology

W = Weather conditions

GP = Government policy

Determinants of supply:

The supply of any commodity is depending upon some factors. They are called determinants of the supply. They are:

i. **Price of the goods:**
Price of the goods is main determinant of supply. Producers supply more goods if the prices are high. They supply the fewer goods when the prices are low.

ii. **Goals of the firm:**
Firms may try to work on various goals for e.g. Profit maximization, sales maximization, employment maximization. If the objective is to maximize profit, then higher the profit from the sale of a commodity, the higher will be the quantity supplied by the firm and vice-versa.

iii. **Inputs Prices:**
The producers supply more when the inputs prices are low, that is at lower costs of production. At higher inputs rises they supply less.

iv. **Technology:**
New Technology generally helps to save inputs and reduces costs and time to produce the output. An improved technology enhances the supply of the goods.

v. **Government Policies:**
Government policy of taxes and subsidies on goods brings about changes in supply, higher taxes on goods discourage producers and their supply will be less. On the other subsidies from government encourage producers to supply more.

vi. **Expectation about future prices:**
If the producers expect an increase in the price of a commodity, then they will supply less at the present price and hoard the stock in order to sell it at a higher price in the near future. This will be opposite in case if they anticipate fall in future price (e.g. Fruit seller).

vii. Prices of the other commodities:

Usually an increase in the prices of other commodities makes the production of that commodity whose price has not risen relatively less attractive we thus, expect that other things remaining the same, the supply of one commodities falls the price of other goods rises.

11. Define elasticity of supply. What are the determinants of elasticity of supply.

Elasticity of supply:

It shows about the proportionate change in the supply and the proportionate change in price. It means it explains how much change in the price and it leads to how much change in the supply.

E_s= Proportionate change in supply/ Proportionate change in Price

$$= \frac{\frac{dq}{q}}{\frac{dp}{p}} = \frac{dq}{dp} \times \frac{p}{q}$$

Types of elasticity of Supply:

There are five types of Supply elasticity of Supply:

1. Perfectly elastic Supply (Es= ∞)
2. Perfectly Inelastic Supply (Es = 0)
3. Relatively elastic Supply (Es > 1)
4. Relatively Inelastic Supply (Es< 1)
5. Unitary elastic Supply (Es = 1)

1. Perfectly elastic Supply (Es= ∞)**:**

When the price is constant if there is a change in Supply it is said to be perfectly elastic Supply. It means the Supply may be increase 'or' decrease without change in price. Here the value of EP is infinity. The Supply curve in this case parallel to X axis.

2. Perfectly Inelastic Supply (Es = 0)**:**

When the price is changed if there is no change in the Supply. It is said to be perfectly inelastic Supply. It means the price may be increase 'or' decrease but the Supply is constant Here the value of Es = 0. The Supply curve in this case parallel to Y axis.

3. Relatively elastic Supply (Es>1):

If the proportionate change in Supply is more than proportionate change in the price. It is said to be relatively elastic Supply. It means a little change in the price leads to more change in Supply. Here the value of Es is greater than one the Supply curve in the case upwards from left to right.

4. Relatively Inelastic Supply (Es <1)

If the proportionate change in Supply is less than proportionate change in the price. It is said to be relatively inelastic Supply. It means a more change in the price leads to less change in Supply. Here the value of Es is less than one. The Supply curve in this case also slopes up wards from left to right.

5. Unitary elastic Supply(Es = 1)

If the proportionate change in the supply is equal to the proportionate change in the price. It is said to be unitary elastic supply. It means the change in the supply and change in price are same. Here the value of Es is 1. Unitary elastic supply curve also slopes downwards from left to right.

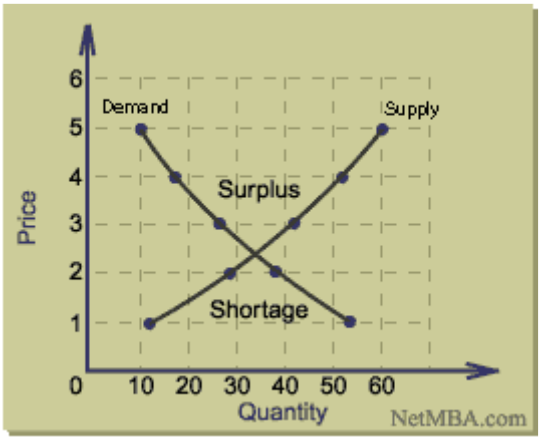
Determinants of elasticity of supply:-

1. Nature of the commodity
   If the good is durable the elasticity of supply will be more [$E_S > 1$], the perishable goods have less elastic [$E_s < 1$].

2. Time factor
   In the long period the elasticity of supply will be more [ES > 1] in the short period the elasticity of supply will be less [$E_S<1$].
3. Availability of facilities
   If they are more facilities [$E_S>1$] (or) [$E_S<1$].
4. Cost of production
   If the cost of production is more the elasticity of supply will be less, if the cost of production is less [$E_S>1$].
5. Nature of inputs
   If the inputs are available in the market there is a more elastic supply otherwise less elastic supply.
6. Risk taking
   If the entrepreneur takes the risks the elasticity of supply will be more otherwise less.

12. Explain how equilibrium price is determined in the interaction of demand and supply.

Equilibrium price means constant price (or) unchanged price. According to classical economists the price of a good is determined by the combined actions of the buyers and sellers. It is nothing but demand and supply. It is actually the price at which the quantity demanded of a commodity equals the quantity supply. This can be explained by the following diagram.



In the above diagram equilibrium price is determined through interaction of demand and supply. Above the equilibrium price there is an excess supply so equilibrium price will fall. Similarly below the equilibrium, there is an excess demand. So equilibrium price will rise.

SECTION – A : ECONOMICS
Study Note – 3
Theory of Production

Learning Objective:

In this Chapter, Theory of production are discussed, which is an effort to explain the principles by which a business firm decides how much of each commodity that it sells and it will produce, and how much of each kind of labour, raw material, fixed capital good, etc., that it employs. The chapter discuss some of the most fundamental principles of economics.

I. Choose the correct answer:

1. …….. is the functional relationship between physical inputs (i.e. factors of production), and physical outputs (i.e. quantity of good / service produced)

(a) Input- Output Function

(b) Demand – Supply Function

(c) Production Function

(d) Cost Function

2. Variable factor means those factors of production-

(a) Which can be only changed in the long run

(b) Which can be changed in the short run

(c) Which can be never be changed

(d) All of the above

3. All Factor of production become variable in

(a) Medium – run

(b) Short- run

(c) Long –run

(d) none of the above

4. What is the maximum point of TP?

(a) When AP become zero

(b) When MP become zero

(c) At the intersecting point of AP& MP

(d) None of these

5. At the point of Infixion, TP will generally
   (a) Show increasing trend
   (b) Show decreasing trend
   (c) Equal to Zero
   (d) be negative

6. If the Marginal product of labour is below the Average product of Labour, it must be true that
   (a) The Marginal product of Labour is negative
   (b) The Marginal Product of Labour is Zero
   (c) The Marginal Product of Labour is falling
   (d) The Average product of Labour is negative

7. Why does the Law of Increasing Returns operate?
   (a) Full use of Fixed Indivisible Factors.
   (b) Efficiency of Variable Factors.
   (c) Need to reach the right combination
   (d) All of the above

8. A Rational Producer will operate in –
   (a) Stage I
   (b) Stage II
   (c) Stage III
   (d) All of the above

9. Internal Economies and Diseconomies arise due to –
   (a) Overall industry-level changes
   (b) Changes at the Firm Level
   (c) Both (a) and (b)
   (d) Neither (a) nor (b)

10. Identify the correct statement.
   (a) Average product is at its maximum when Marginal Product is equal to Average Product.
   (b) Law of Increasing Returns to Scale relates to the effect of changes in factor proportions.
   (c) Economies of Scale arise only because of invisibilities of factor proportions.
   (d) labour supply curve is strictly upward rising

Answer.

1. C
2. B
3. C
4. B
5. A
6. C
7. D
8. B
9. B
10. A

II. Fill in the blanks:

1. **------ is the factor of production that is limited in supply.**
2. **The shape of supply curve of labour is ----------**
3. **----- is called produced means of production**
4. **When total product is diminishing marginal product will be ------**
5. **In the long run all factors of production are ---- factors.**
6. **When output increases more than the increase in inputs, it is ------- returns to scale**
7. **The law of variable proportion is also called the law of ----------**
8. **Average product is maximum when ----------**
9. **The concept ‘ returns to scale’ is applicable in the --------**
10. **The person who is engaged in production related decision making is called ----------**

Answer.

1. Land
2. Backward bending
3. Capital
4. Negative
5. Variable
6. Increasing
7. Diminishing marginal returns
8. AP=MP
9. Long Run
10. Entrepreneur

III. State the sentence true or false

1. **Production function explains the relationship between inputs and output ( )**
2. **The factors that are available in the short period are called fixed factors ( )**
3. **When the marginal product is divided with number of unity labour then AP can be obtained ( )**
4. **Imperfect substitution is one of the reasons for diminishing marginal returns ( )**
5. **When the TP is maximum, then the AP is zero ( )**
6. **Use of capital helps to provide improved transportation facilities ()**
7. **Labour is a perishable good that cannot be preserved ()**
8. **When average product is increasing marginal product lies below the average product curve ()**
9. **The law of diminishing returns is associated with the factor capital ()**
10. **Average product is rising but marginal product is falling in stage II ()**

Answer.

1. T
2. T
3. F
4. T
5. F
6. T
7. T
8. F
9. F
10. F

IV. Matching:

1. Fixed factor	**A. increasing returns**
2. Land	**B. Specialisation of labour**
3. Σ mp	**C. Stage II production**
4. Indivisible factors	**D. Long run**
5. Law of Variable Proportion	**E. Diminishing returns**
6. Returns to scale	**F. short period**
7. Rising MP and AP	**G. Distribution of factor income**
8. Rise in input prices	**H. total product**
9. Increasing returns	**I. Alfred Marshall**
10. Entrepreneur	**J. fixed factor**

Answer.

1. F
2. J
3. H
4. A
5. I
6. D
7. C
8. E
9. B
10. G

V. Answer the following questions

1. What is production?

Generally production means a process to change the raw materials into final goods (or) finished goods. But in economics making of the goods (or) creation of goods (material and immaterial) for the purpose of selling them in the market is called production.

2. Define a production Function.

Production function expresses the relationship between the physical inputs and physical output of a firm for a given state of technology. The production-function is a purely technical relation that connects factor-inputs and outputs. The production-function can be written mathematically as follows:

$Qx = f (F_1, F_2, F_3 \ldots\ldots\ldots F_N)$

Here, Q_x = the quantity of x commodity, $F_1, F_2, F_3 \ldots\ldots\ldots F_N$ = different factor-inputs. This equation tells that the output of x depends on the factor $F_1, F_2, F_3 \ldots\ldots\ldots F_N$ etc. Clearly There is functional relationship between factor-inputs and the amount of goods x.

3. What are the types of production function?

Based on the duration of production, production functions are of two types:

A. Short period production functions:

It shows the relationship between production and factors of production in the short period. In the short period all factors may not be available, so the factors of production in the short period can be divided into two types they are:-

i. Fixed factors

ii. Variable factor

i. **Fixed factors:**
The factors which are not available in the short period they can be kept as constant. So they are called fixed factors. **Example:** land, building, machines etc.

ii. **Variable factors:**
The factors which are available to change the output in the short period, they can be changed so they are called variable factors. **Example:** capital, labour, raw materials etc.

B. Long period production function:

It explains the relationship between production and factors of production in the long period. It is also called as law of return to scale. In this regard, it should be noted that the classification of fixed and variable factors is related to only short period. But in long period all factors are variable factors.

4. What is land and explain the features of land?

Land in common usage is soil or surface of the earth. As a factor of production it refers to all natural resources like forests, water, climate, minerals etc. It mainly supplies food to people, provides space for work and supplies raw material to industry. Land has certain peculiar features:

i. **Gift of nature:**
Land is a gift of nature. Location of land deposits of minerals at certain places. Climatic conditions are no doubt gift of nature.

ii. **Limited in supply:**
The total geographical area of a country remains the same. In fact certain resources like oil, gas, coal and some species of wild life may not be available after some time.

iii. **Immobile factor:**
Land cannot be moved from one place to another like other factor. However its ownership can be transferred and its use can be shifted from one crop to another crop.

iv. **Diminishing returns:**
Early economists held the view that land is subject to the law of diminishing returns. Increased use of capital and labour on any given quantity of land would give us diminishing returns.

v. **Land differs in fertility:**
There will be differences in fertility of land. As a result, the output changes from one plot to the other. It is because of these peculiarities of land, the early economists considered land as a separate factor of production.

5. What is Labour and explain the features of labour ?

In the ordinary usage, labour stands for only physical labour. In economics, labour means physical as well as mental services engaged in production to earn income. Classical economists and Karl Marx have considered labour as the sole factor of production. Labour as a factor of production possesses certain peculiar features:

i. **Labour is inseparable**: Labour is inseparable from labourer but in the case of other factors i.e. land and capital are separable from land lord and capitalist.

ii. **Labour is perishable**: If a worker does not find work on a particular day, the labour is lost for that day. Like other factors of production, labour cannot be preserved.

iii. **Supply of labour**: Labourers offer more labour at lower wages. When wages rise beyond a certain level they prefer to enjoy leisure and supply less labour. It is observed that supply curve of labour is backward bending at higher wages.

iv. **Weak-bargaining power**: Labour has less bargaining power as it is a perishable thing. In the same way the trade unions are not strengthened so they cannot fight for better wages.

v. **Differ in efficiency of labour**: Some labourers have more efficiency and some labourers have less efficiency.

6. What is Capital and explain the functions of capital?

In the ordinary sense capital means money for an individual or a firm. Money is a form of capital when it is used to purchase machinery, tools, raw materials etc. However, it should be noted that machinery, tools etc are basically man made goods that help in the production of goods. These are vital in raising productivity in different sectors. Capital performs certain important functions in production.

i. Capital supplies tools and machines that assist the labourers in working efficiently and producing more output. A labourer backed by better tools and machines will be more efficient in production.
ii. Improves productivity of labourer. This in turn increases the overall production.
iii. Capital supplies raw materials on continuous basis that is required in production.
iv. Additional tools and machines generate more employment to people. However in the modern production, labour replacing machines reduce employment opportunities.
v. Capital in the form of roadways, railways, ships help to transport raw material to the site of the production and finished goods to the market.
vi. Capital in the form of money is useful for the payment of advance wages to the labourers even before the goods are sold in the market.

7. What is and Organization explain the functions of Organization?

The person who organizes the production is called an entrepreneur. He is considered as a separate factor because he performs specific functions different from those of other factors. Now-a-days an entrepreneur is not considered as a separate factor but as special types of human labourer. Whenever the ownership and the management are one and the same entrepreneur has to perform certain specific functions.

Functions of the entrepreneur:

i. Entrepreneur has to initiate the business by mobilizing other factors. All the primary work to start the business will be undertaken by him.

ii. Major decisions like the kind of good to be produced, size of the unit, quantity of output, price, marketing etc. have to be made by him. Choosing the technology:

iii. Choosing suitable technology, combining factors in right proportion to maximize output at minimum cost are the other functions of organizer.

iv. He must be dynamic to introduce new methods, techniques, products etc.

v. As entrepreneur he has to pay the rewards to other factors. He has to bear the responsibility either for profit or loss in production.

8. Explain the law of variable proportions. Distinguish between total product, average product and marginal product with the help of this law.

This law was developed by Alfred Marshall. It explains the relationship between inputs and outputs in the short period. According to this law, output can be increased at a less than proportionate rate by increasing the some factors (variable factors) while other factors are constant. So it is called the law of variable proportions.

Total product: It refers to the total output of the firm per period of time when one input is changed while other inputs are kept unchanged.

Average Product - Average Product is total output per unit of the variable input. Thus Average Product is total product divided by the number of units of the variable factor.
$AP_L = TP_L / L = Q/L$ where Q is Total Product, L is the quantity of labour.

Marginal Product - Marginal Product is the change in total product resulting from using an additional unit of the variable factor. Assuming labour as the variable factor we can write,
$MP_L = dQ/dL$ where d is the rate of change.
Alternatively we can write $MP_L = \Delta TP_L / \Delta L = TP_n - TP_{n-1}$. Total product can be abtained by adding all marginal productivities of labour.
Tabular Explanation: The concept of total product, average product and marginal product can be explained with the help of following table.

Table 1

Units of labour	Total product	Average product	Marginal product
1	10	10	10
2	22	11	12
3	36	12	14
4	48	12	12
5	55	11	7
6	60	10	5
7	60	8.6	0
8	56	7	-4

Table 1 shows that in the initial stage (stage1) total product, average product and marginal product are increasing. This stage is called increasing returns. In the second stage (stage 2) total product is increasing but average and marginal product start falling. In the third stage, total product starts falling and marginal product becomes negative. This is the stage of decreasing returns.

Diagrammatic Explanation:

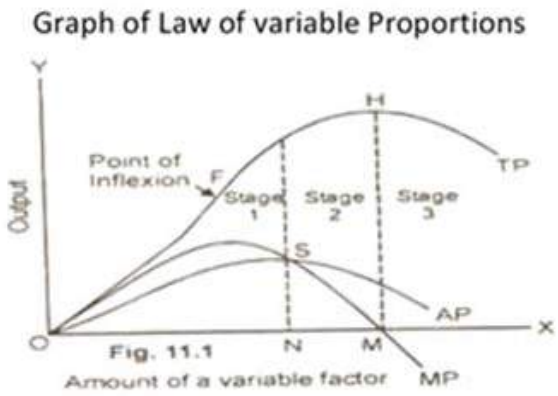


Figure: 1

Main points in this law:

- In stage I, the T.P., A.P., M.P. go on increasing but at the end of the 1st stage M.P starts to decline. The 1st stage ends when the M.P. is equal to A.P.
- In the stage II, T.P. goes on increasing but it increases with diminishing rate. A.P. goes on diminishing. M.P. also goes on diminishing at the end of the 2nd stage the T.P reached the maximum. When the T.P is maximum then the M.P is zero. It intersects the x-axis.
- In the stage III, the T.P. and A.P. go on diminishing but for the M.P. becomes negative so the M.P. curves crossed the x-axis.
- The M.P. curve intersects the A.P curve when the A.P is maximum.
- The law of variable proportions is also called "law of diminishing marginal returns".
- This law is not only applicable to agriculture sector but also applicable to industrial sector, service sector etc.

Reasons for the diminishing returns:

- All units of variable factors are not homogenous.
- Imperfect substitutions.
- The combination becomes wrong.

Importance:

- This law is useful to firm (or) producer for the decision making regarding the output.
- According to this law the firm (or) producer operates only in second stage. He never chooses the either first stage (or) third stage.

Assumptions:

- The units of the variable factor are homogenous.

- There is a possibility to change the some factors (Variable factors), while other factors are constants (fixed factors).
- There is a possibility to change the combination of fixed and variable factors.

- There must be no change in the level of technology.
- It is applicable to only short period.

9. Explain the law of returns to scale.

It shows the relationship between inputs and outputs in the long period. The change in the quantity of the factors is called scale. Change in the output is called returns. So law of returns to scale explains changes in the output due to changes in the inputs in the long period when all inputs are changed in the same quantity.

Explanation of the law:

According to this law when all inputs are increased in same proportions when the output is not increased in the same proportion. The changes in the output are classified in to three stages. They are

- Increasing returns to scale
- Constant returns to scale
- Diminishing returns to scale

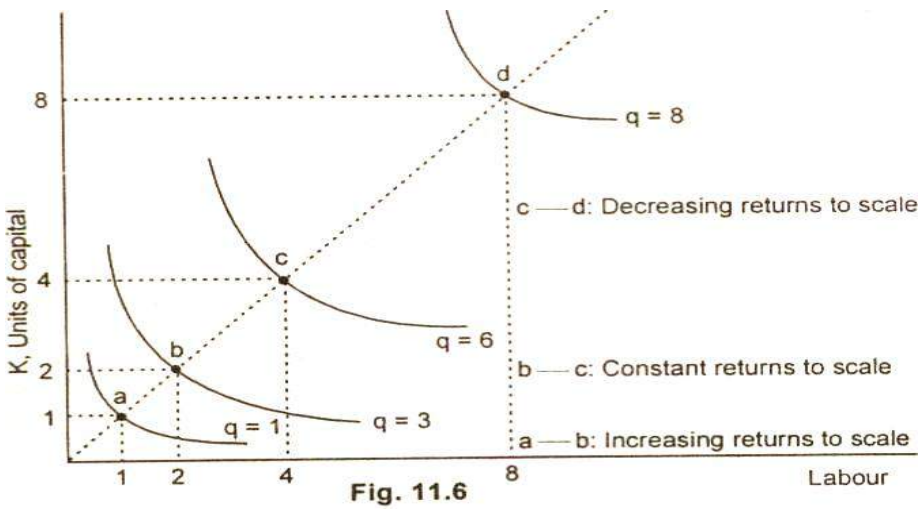


Figure: 2

Increasing returns to scale:

If the proportionate increase in the output is more than proportionate increase in the inputs it is said to be increasing returns to scale. It means when we double the inputs the output will be more than double.

Cause for increasing returns:

1. Specialization (or) Division of labour
2. Indivisible factors.

3. Dimensional economics
4. Volume discounts etc.,

Constant returns to scale:

If the proportionate increase in the output and proportionate increase in the inputs are same it is said to be constant returns to scale. It means when we double the inputs the output also will be double.

There are no causes for constant returns. It is just an indicator for the ending of increasing returns and commencement of diminishing returns.

Diminishing returns to scale:

If the proportionate increase in the output is less than proportionate increase in the inputs it is said to be diminishing returns. It means when we double the inputs the output will be less than double.

Cause for diminishing returns:

a. Management problems.
b. Limit to human factor
c. Lack of corporation and co-ordination
d. Rise of the prices of inputs

10. Distinguish between Returns to a Variable Factor (or Law of Variable Proportions) and Returns to Scale.

The main differences between returns to a variable factor and returns to scale are as indicated below:

a. Returns to a variable factor operates in the short run or it is related to short run production function. However, returns to scale operate in the long-run or it is related to long run production function.

b. Under returns to a variable factor, only the quantities of a variable varied. However, under returns to scale all factor-inputs are varied in the same proportion.

c. Under returns to a variable factor, there is change in the factor-proportion. Suppose on 1 acre land 1 labour is employed, then the land labour ratio is 1 : 1. Now if we add one more unit of labour on the 1 acre land, then land-labour ratio would become 1 : 2. However, under returns to scale there is no change in factor-ratio. For instance, if a firm is employing 1 unit of labour and 2 units of capital, then the labour-capital ratio is 1 : 2. Now if the firm increases its scale of operation and employed 2 units of labour and 4 units of capital, the labour-capital ratio still remains the same as 1 : 2.

d. Under returns to a variable factor, no change take place in the scale of production. Because here all the factor inputs are not changed. However, under returns to scale there is change in the scale of production because here all the factor inputs are varied.

SECTION – A : ECONOMICS
Study Note – 4
Theory of Cost

Learning Objective:

The firm's costs determine its supply. Supply along with demand determines price. To understand the process of price determination and the forces behind supply, we must understand the nature of costs. In this Chapter, some important concepts of costs, and traditional and modern theories of costs are discussed.

I. Choose the correct answer

1. The cost function shows the functional relationship between cost of production with ---------
- **(a) Output produced by the firm**
- **(b) physical quantity of inputs**
- **(c) revenue earned by the firm**
- **(d) prices of inputs used in production**

2. Implicit cost is also called ----------
- **(a) nominal cost**
- **(b) imputed cost**
- **(c) real cost**
- **(d) opportunity cost**

3. Payments made to the factors of production is called
- **(a) Implicit cost**
- **(b) explicit cost**
- **(c) accounting cost**
- **(d) both (b) and (c)**

4. Average fixed cost curve is a
- **(a) Downward sloping curve**
- **(b) downward sloping straight line**
- **(c) rectangular hyperbola**
- **(d) none of the above**

5. When output is zero which of the following statement is true?
   (a) Short run total cost is zero
   (b) total fixed cost is zero
   (c) total variable cost is zero
   (d) none of the above

6. Marginal cost is defined as
   (a) Changes in total cost
   (b) changes in total variable cost
   (c) either (a) or (b)
   (d) none of the above

7. When average cost is falling what will be the position of marginal cost?
   (a) MC lies below AC
   (b) MC lies above AC
   (c) MC intersects AC
   (d) none of the above

8. Suppose total cost curve is given by the equation $C = 5 + 4q$. In this case
   (a) AC>MC
   (b) AC<MC
   (c) AC =MC
   (d) either a or b

9. In case of internal economies of production, long run average cost curve will be
   (a) upward rising
   (b) downward sloping
   (c) constant
   (d) both a and b

10. As a result of external economies of production LAC curve will
   (a) shift upward
   (b) shift downward
   (c) either a or b
   (d) remain unchanged

11. Suppose the revenue function is given by: $R = 7Q$. In this function
   (a) Average Revenue>Marginal Revenue
   (b) Average Revenue<Marginal Revenue
   (c) Average Revenue=Marginal Revenue
   (d) either (a) or(bi)

12. Under perfectly competitive market
   (a) MR curve is parallel to horizontal axis
   (b) MR curve is downward sloping
   (c) MR curve is upward rising
   (d) parallel to vertical axis

13. Under imperfect market structure

(a) Price= Marginal Cost

(b) Price>Marginal Cost

(c) Price < marginal cost

(d) price is unrelated to marginal cost

14. When constant returns to scale operates, short run average cost becomes tangent to long run average cost

(a) In the falling portion of LAC

(b) at the min. point of LAC

(c) in the rising portion of LAC

(d) either (b) or (c)

15. Which of the statement is true regarding short run cost

(a) Both AC and AVC are u shaped

(b) AC is U shaped but AVC is falling

(c) AC is falling but AVC is U shaped

Answer.

1. (a)
2. (b)
3. (d)
4. (c)
5. (c)
6. (c)
7. (a)
8. (a)
9. (b)
10. (a)
11. (c)
12. (a)
13. (b)
14. (b)
15. (a)

II. Fill in the blanks

1. **_____ curve never touch the x-axis**
2. **Costs which do not involve any cash payment to outsides are called _____**
3. **Accounting costs equal to _____ costs.**
4. **_____ cost must be paid even if the firm's level of output is zero.**
5. **When the total revenue equal to economic costs then the firm will earn _____**
6. **TC_n - TC_{n-1} is equal to _____ cost**
7. **ATC curve will be in _____ shaped.**
8. **The vertical difference between TVC and TC is equal to _____.**
9. **When the AC=MC then the average cost is _____**
10. **Variable cost obeys the law of _____ in the short run.**
11. **Long run average cost is the _____ of short run average costs**
12. **Economic cost is the sum of explicit cost, implicit cost and _____**
13. **Under imperfect competition, both AR and MR will be _____**
14. **Division of labour and specialisation will result in_____ economies in production.**
15. **In the long run, each short run average cost represents a _____**

Answer.

1. AFC
2. Implicit cost
3. Explicit
4. Fixed
5. Normal profit
6. marginal
7. 'U' shaped
8. Total Fixed Cost
9. Minimum
10. Returns to variable proportion
11. Envelope
12. normal profit
13. downward Sloping
14. Internal
15. Plant Size.

III. State the sentence true or false

1. **Cost function explains the relationship between inputs and output ( )**
2. **The fixed cost is apart of short runcost only ( )**
3. **When the total cost is divided by the number of output, Average Cost (AC) can be obtained ( )**
4. **Average Fixed Cost remain fixed with increase in output ( )**
5. **Marginal Cost is greater than average cost when average cost is falling ()**
6. **The main cause for the 'U' shape of LAC curve is internal economics and internal diseconomies ( )**
7. **As a reason of external economics the LAC curve shifts upwards ( )**
8. **Short run total cost is zero when output is zero ()**
9. **In perfect market AR=MR curve is parallel to x-axis ( )**
10. **In imperfect market MR curve is a below the AR curve ( )**
11. **Long run marginal cost intersects Long run average cost when LAC is at its minimum ()**
12. **In perfect market and imperfect market the price is equal to average revenue. ( )**
13. **In the long run when internal economies are existent, plants are overutilised ()**
14. **Economic cost is also called accounting cost ()**
15. **The discrepancy between price and marginal revenue is the unique feature of imperfect competition ()**

Answer.

1. F
2. T
3. T
4. F
5. F
6. T
7. T
8. F
9. T
10. T
11. T
12. T
13. F
14. F
15. T

IV. Matching:

1. Fixed factor	**A. increasing returns**
2. Land	**B. average cost**
3. Σ mp	**C. opportunity cost**
4. Indivisible factors	**D. economic cost**
5. Implicit cost	**E. LAC curve**
6. Normal profit	**F. short period**
7. National priorities	**G. real cost**
8. Planned curve	**H. total product**
9. AFC+AVC	**I. rent to own land**
10. Waiting of sacrifices	**J. fixed factor**
11. Average fixed cost	**K. Internal Diseconomies**
12.External Economies	**L. Fixed Cost**
13. Short Run	**M. Technological Improvement**
14.Insurance Premium	**N. Rectangular Hyperbola**
15. Change in taste and preference	**O. Fixed Plant Size**

Answer.

1. F
2. J
3. H
4. A
5. I
6. D
7. C
8. E
9. B
10. G
11. N
12. M
13. O
14. L
15. K

V. Answer the following Questions:

1. What is meant by cost of production? Explain the types of costs.

It is the expenditure incurred by the producer (or) firm to produce the goods and services. Hence cost can be expressed as a function of output: C = f(Q).

Types of cost:

a. Nominal Cost:

If the remunerations of the factors of production are paid in the form of money it is called nominal cost.For example: rent paid to the land, wages to the labourers etc.

b. Real cost:

The concept of real cost was introduced by Alfred Marshall. Exertions of all kinds of labour that arealready indirectly involved in production process. All these efforts and sacrifices together will be calledas real cost of production. For example exertions of all kinds of labour, waiting and sacrifices requiredfor saving the capital.

c. Economic costs:

Total expenses incurred by a firm (or) producer in producing a commodity are called economic costs. These economic costs includes

(i) Explicit costs
(ii) Implicit costs
(iii) Normal profit.

Explicit costs:

Actual payments made by a firm for purchasing or hiring resources are called explicit costs. These costsare actual money expenses directly incurred for purchasing the resources for example rent to the land, wages to the labourer, expenditure on raw material interest on borrowed money etc.,

Implicit costs:

These costs are imputed costs of the factors of productions owned by the producer himself which aregenerally left out in the calculation of expenses of the firm. For example rent for the use own land,interest on his own capital etc.

- Explicit costs are recorded in the account books but implicit costs are not recorded.
- Explicit costs are also called "Accounting costs"

Normal profits:

The minimum amount which is required to keep an entrepreneur in the production process is known as normal profit.

- Economic cost = Explicit cost + Implicit cost + normal profits.

d. Opportunity cost:

The opportunity cost of anything is next best alternative cost that is forgone. Individual point of view (or) nation point of view the resources are scarce. At that time to get the one commodity we have to forgo the another commodity. This is called opportunity costs.

Suppose a price of land can be used for growing wheat or rice. If the land is used for growing rice, it is not available for growing wheat. Therefore the opportunity cost for rice is the wheat crop foregone.

2. Define opportunity cost. State the importance of opportunity cost.

Since resources are limited/scarce, every time we make a choice about how to use them, we also choose to forego other options. Economists use the term opportunity cost to indicate what must be given up to

obtain something that is desired. The idea behind opportunity cost is that the cost of one item is the lost

opportunity to consume something else. In short, the opportunity cost is the value of the next best alternative. Suppose a land can be used for growing wheat (product A) or rice (product B). If the land is used for growing rice, it is not available for growing wheat. Therefore the opportunity cost for rice is the wheat crop foregone. This is illustrated with the help of the following diagram.

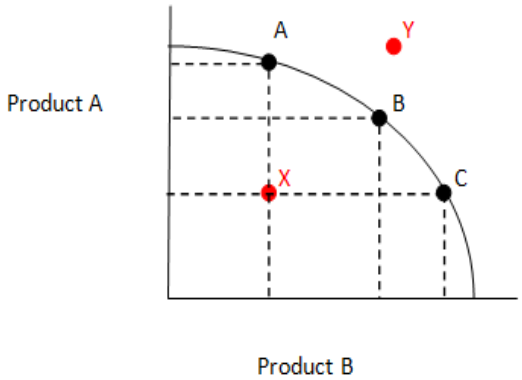


Figure: 1

Figure 1 shows that points A,B,C etc. determine different combinations of two products feasible for the firm to produce. They are scalled Pareto Efficient Points because resources are fully utilized here. Point X is inefficient point, as resources remain unutilized. On the contrary, point Y is desirable but not feasible for the firm.

Applications of Opportunity cost

The concept of opportunity cost has been widely used by modern economists in various fields.

i. **Determination of factor prices:**
The factors of production need to be paid a price that is at least equal to what they command for alternative uses. If the factor price is less than factor's opportunity cost, the factor will quit and get employed in the better-paying alternative.

ii. **Determination of economic rent:**
The concept of opportunity cost is widely used by modern economists in the determination of economic rent. According to them, economic rent is equal to the factor's actual earning minus its opportunity cost (or transfer earnings).

iii. **Decisions regarding consumption pattern:**
The concept of opportunity cost suggests that with given money income, if a consumer chooses to have more of one thing, he has to have more of one thing; he has to have less of the other. Hence with the help of opportunity cost he decides the consumption pattern, that is, which goods should be consumed and in what quantities.

iv. **Decisions regarding production plan:**
With given resources and given technology if a producer decides to produce greater amount of one commodity, he has to sacrifice some amount of another commodity.

v. **Decisions regarding national priorities:**
If a country decides that more resources must be devoted to arms production then less will be available to produce civilian goods. In this situation a choice will have to be made between arms production and civilian goods. The concept of opportunity cost helps in making such choices.

3. Distinguish between fixed costs and variable costs

Short run costs: In the short period cost of production can be divided into two types. They are i. Fixed costs ii. Variable costs

A1. Fixed costs: The costs which don't change with change of the output are called fixed costs. It means output may be increase (or) decrease but no change in these costs. Irrespective of the Level of output Quantity the producer must incur this cost. Even the output is zero the fixed cost is positive. The fixed cost curve (TFC) will be parallel to x-axis. Example: expenditure on the land, building, salaries of permanent employees, interest payment, insurance premium etc.

A2. Variable costs: Costs which changed with change of the output quantity are called variable costs. It means when the output is increased, these costs increased and when the output is decreased, these costs are also decreased. When the output is zero these costs are also zero. The TVC curve will be sloped upwards from "left to right" And it is started from the origin. Example: Expenditure on raw material, power, fuel, wage of daily laborers etc. We can list the difference between fixed and variable cost as follows:

a. Fixed costs do not vary with quantity of output. However, variable costs vary with the quantity of output. B. Fixed costs are related with the fixed factors while variable costs are related with the variable factors. C. Fixed costs do not become zero. They remain same even when production is stopped. However, variable costs can become zero when production is stopped D. A firm can continue production costs are not recovered even fixed costs. However, production should at least recover the variable cost in order to stay in production.

4. Explain short run costs with suitable diagrams

In the short period cost of production can be divided into two types. They are a. Fixed costs b. Variable costs. Fixed cost is defined as the cost with does not vary with level of output. While variable cost varies with level of output. WE can represent these two costs with the help of following diagram.

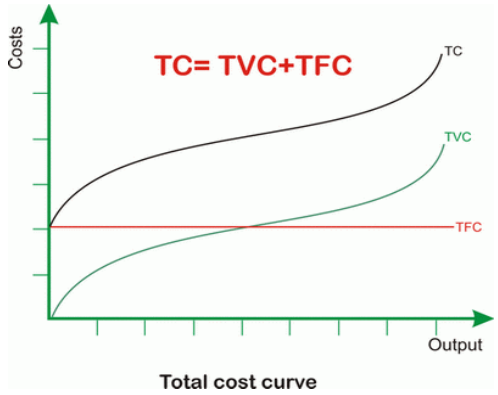


Figure: 2

Figure 2 shows that TFC curve is parallel to the horizontal axis showing invariance of the Total Fixed Cost (TFC) with respect to output. However, Total variable cost (TVC) curve is increasing following law of variable returns to proportion. Joining TFC and TVC we get Short run total cost (TC) which will be of same shape as TVC – it is increasing at an increasing rate and then increasing at a decreasing rate. However, unlike TVC, TC will have a positive vertical intercept showing the amount of TFC.

Average fixed cost:

It is the average total fixed cost per unit of output when TFC is divided with no. of units of output AFC can be obtained

AFC= TFC/Q.

• The AFC curve slopes downwards from left to right and it is Rectangular hyperbola.

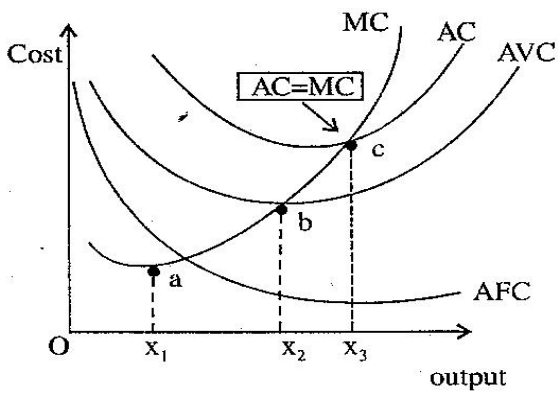
Average variable cost:

It is the average total variable cost per unit of output when the TVC are divided with no. of units of output AVC can be obtained

AVC=TVC/Q

• The AVC curve will be in 'U' shape

Now, Average cost is defined by AC=TC/Q. Further, AC= AFC + AVC. All three curves are shown in figure 3.



Relationship Digram Between AVC & MC, AC & MC

Figure: 3

Figure3 shows that AFC curve is monotonically decreasing but it never touches the x axis. Such curve is called rectangular hyperbola because area under the curve (that represents total fixed cost) always remain constant although average fixed cost is falling continuously. Further, AVC curve is U shaped showing following law of variable returns to proportion. Joining AVC and AFC we get AC curve which is also U shaped.

Marginal Cost

It is the additional cost to produce the additional unit of a thing (or) one more unit of a thing. The change in the total cost is also called marginal cost.

$$MC=\Delta TC/\Delta Q=TC_n-TC_{n-1}.$$

shows that MC curve is also U shaped. Further, it is found that MC curve touches both AVC curve and AC curve at their respective minimum point.

5. Explain the difference between average cost and Marginal cost. In this respect mention the relationship between average cost and marginal cost.

Average cost:

It is the average total cost per unit of the output. When the total cost is divided with no. of units of outputs AC can be obtained. AC= TC/Q. The average total cost curve is 'U' shaped.

Marginal cost:

It is the additional cost to produce the additional unit of a thing (or) one more unit of a thing. The change in the total cost is also called marginal cost. $MC=\Delta TC/\Delta Q=TC_n-TC_{n-1}$. Marginal cost curve is also 'u' shaped.

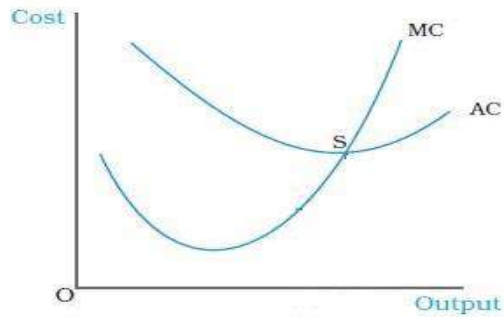


Figure: 4

Figure 4 shows average cost and marginal cost curves. It is seen that both curves are u shaped. Moreover, it is found that when average cost is falling, marginal cost is less than the average cost. Similarly when average cost is rising, marginal cost is greater than average cost. Lastly, when average cost is minimum, marginal and average cost are equal to each other. So the former intersect the average cost at its minimum point.

6. Explain long run average costs with suitable diagrams. Why long run average cost is called an "envelope" of short run average costs?

Long run is a period of time when all factors of production are variable. Here, a producing firm will experience returns to scale in production. Returns to scale are of three types: i. increasing returns ii. Constant returns iii. Decreasing returns. Accordingly, long run average cost will be falling, remain constant or rising depending on the nature of returns to scale. This is shown in the following diagram (figure 5).

Further, in a short period a firm has a fixed scale of plant the short run average cost curve corresponding to a particular scale of plant. So in short period the firm can operate on a particular scale of plant. But in the long run a firm can choose among possible sizes of plant (or) it can move from one scale of plant to another scale of plant. This is also by the following diagram (figure 5).

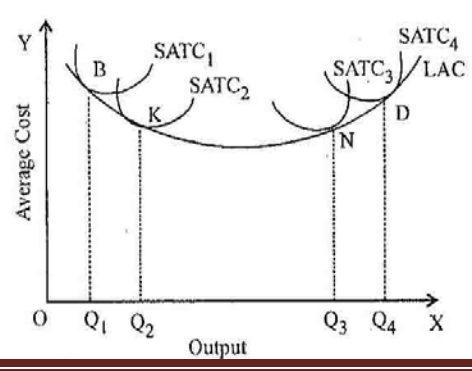


Figure: 5

In the above diagram it is found that LAC curve will be U shaped. When firm experiences increasing returns to scale long run average cost will be falling. Similarly, LAC will be rising in case firm is experiencing decreasing returns. Hence LAC will be U shaped.

Now in the long run there are various short run average cost curves which correspond various sizes of plant. The LAC curve will be tangent to each of the short run AC curve. It shows the least possible AC producing a quantity of the output when scale of plant is varied. This is the reason LAC curve is called an envelope of all SACs.

7. State the internal economies and diseconomies of large-scale production. What are the impacts of internal economies on long run cost?

Economies of scale are the reduction in per unit cost of production as the volume of production increases. When the output is carried on larger quantities there are some advantages. These advantages are called economies of the large scale production. These economies are divided in to 2 types. They are: a. Internal economies b. External economies

Internal Economies:
When a firm expands its size of business (or) increases its output, it gets some advantages. They are called internal economies. These internal economies are related to a single firm and not related to all other firms in the industry.

Types of the internal economies:

i. Labour economies:
Division of labour and specialization are possible more in large-scale operations. Different types of workers can specialize and do the job for which they are more suited. As a result of this quality and speed of work both improve.

ii. Technical economies:
A large firm will be able to install large capacity of machines in place of small sized machines. It also adopts latest technologies. These will give mechanical advantage over small firms and costs will be minimum.

iii. Managerial economies:
Highly talented managers of specialized skills will be employed by large firms. It helps to makes better decisions in the production.

iv Marketing economies:
Large scale purchase of raw materials and sale of finished goods gives the advantage of transport concessions to the firm. Advertisement costs will be less due to large output sales.

v. Financial economies:
Large firms will be able to borrow credit easily. These firms will be able to offer securities and their goodwill in the market enables them to borrow at reasonable rate of interest. They also raise capital by attracting investors.

vi. Research and Development:
Improvements in technology efficient use of resources improvement in quality of products depend on research. Only large firms can afford to bear the expenditure on research.

vii. Economies Related to Transport and Storage costs:

Large firms are able to enjoy freight concession from railways and road transport. Because a large firm uses it s own transport means and large vehicles, the per unit transport costs would fall. Similar, a large firm can also have its own storage go downs and can save storage costs

viii. Risk bearing economies:

Generally large firms diversify their production into different goods and services. Therefore, even if there is a loss in one item of good it can be covered by profit in other goods.

Internal diseconomies:

Internal diseconomies are those disadvantages which are internal to the firm and accrue to the firm when it over expands its scale of production. The main internal diseconomies of scale are as follows:-

i. Management diseconomies

These diseconomies occur primarily because of increasing managerial difficulties with too large as scale of operations. It becomes difficult for the top management to exercise control and to bring about proper coordination.

ii. Technical diseconomies

If a firm frequently changes in it technologies and used new technologies and new machines, it may increase its costs. After a certain limit, the large size or volume of the plant and machinery may also prove disadvantageous.

iii. Risk bearing diseconomies

The business cannot be expanded indefinitely because of the principle of increasing risk. The risk of the firm increases because of reduction in demand change in fashion and introduction of new substitutes in the market.

iv. Marketing diseconomies

A large firm is forced to spend more on bringing and storing of raw materials and selling of finished goods in the distant markets.

v. Financial diseconomies

A large firm has to borrow a large amount of money even at higher rate of interest. It imposes a burden on the financial position of the firm.

Impact of internal economies and internal diseconomies on LAC curve:

When a firm accrues internal economies with the expansion of its scale of output, the LAC curve would fall. And when after a certain point, a firm receives internal diseconomies with the expansion of its scale of output, the LAC curve would rise.

Thus, internal economies causes the LAC to fall and internal diseconomies cause the LAC to rise. Hencethe internal economies and diseconomies are responsible for the U-shaped of the LAC curve. It is shown in the diagram.

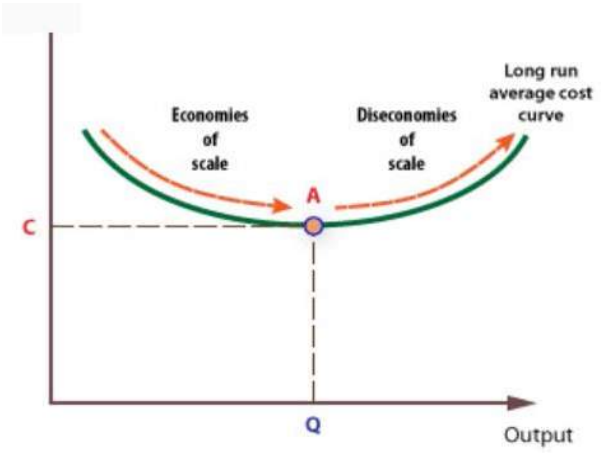


Figure: 6

8. State the external economies and diseconomies of large scale production. What are the impacts of external economies on long run cost?

Economies of scale are the reduction in the per unit cost of production as the volume of production increases. When the output is carried on larger quantities there are some advantages. These advantages are called economies of the large scale production. These economies are divided in to 2 types. They are: a. Internal economies b. External economies

External Economies:
Firm is a unit, the group of firms is called industry. When industry is expended they are some advantages. These advantages are enjoyed by all the firms in the industry so they are called external economies. These economics are opened for all the firms it means they are not related to a single firm.

Types of external economies:

i. Economies of localization (or) concentration
Location of several firms at one place makes available certain facilities. Local authorities may develop roads, communication, power, irrigation etc. Other facilities like banking, insurance, skilled labour will come up in the area. These arrangements benefit all the firms located in that place.

ii. Economies of disintegration (or) specialization
Production of goods can be split into different parts and each firm may take up one part of producing the goods. This will result in specialization and improve performance of each firm in the production. This division of labour helps to produce more output and reduces costs of production.

iii. Economies of related to information services
All the firms in the area are dealing with the same goods. Information can be shared among the firms about raw material, skilled labour, marketing etc. Expenditure on these items can be reduced and there will be mutual advantage to all the firms.

iv. Economies of producers' organization
Collective research by all the firms on new products, technologies will help reduce expenditure. The fruits of research can be enjoyed by all the firms.

External diseconomies:
Diseconomies which accrue to the firms as a result of the expansion in the output of the whole industry are termed external diseconomies. The main external diseconomies are as follows:

i. **Increase in the input prices**
When the industry expands, the demand for factor-inputs increases. As a result the input prices (such as wages, prices of raw materials and machinery equipments, interest rates, transport and communication rates etc.) shoot up. This causes the cost of production to rise.

ii. **Pressure on infrastructure facilities**
Concentration of firms in a particular region creates undue pressure on the infrastructure facilities – transportation water, sanitation, power and electricity etc. As a result, bottlenecks and delays in production process become frequent which tend to raise per unit costs.

iii. **Diseconomies due to exhaustible natural resources**
Diseconomies may also arise due to exhaustible natural resources. Doubling the fishing fleet may not lead to a doubling of the catch of fish; or doubling the plant in mining or on an oil-extraction field may not lead to a doubling of output.

iv. **Diseconomies of disintegration**
When the production of a commodity is disintegrated among various processes and sub-process, it may prove disadvantageous after a certain limit. The problem and fault in any one unit may create limit. The problem and fault in any one unit may create problem for whole of the industry, Coordination among different concerns also poses a problem.

Impact of external economies and external diseconomies on LAC curve:

(i) As a result of external economies, the LAC curve of the firms shifts downwards. It is shown in the diagram below that because of external economies. LAC curve shifts downwards from LAC1 to LAC2. (figure 7)

(ii) As a result of external diseconomies the LAC curve of the firms shifts upwards. It is shown in the diagram below that because of external diseconomies. LAC curve shifts upwards from LAC1 to LAC2 (figure 7).

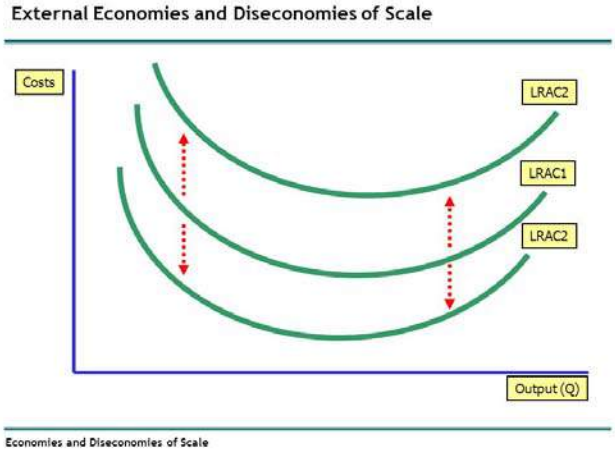


Figure: 7

9. Define Total Revenue, Average Revenue and Marginal Revenue.

1. **Total revenue:**
   It is the total amount of income obtained by the firm 'or' producer by the selling of total goods and services in the market. The sum of all marginal revenue is also called total revenue : TR = PXQ (or) TR = Σ MR

2. **Average Revenue:**
   It is the revenue per unit of output to be sold in the market. When the total revenue divided with no. of units of output AR can be obtained : AR=TR/Q

3. **Marginal Revenue:**
   It is the additional revenue obtained by the firm (or) producer by the selling of additional unit of a output (or) one more unit of a output. The change in the total revenue is also called marginal revenue: $MR = \Delta TR/\Delta Q = TR_n - TR_{n-1}$

Relation Between AR and MR:

When average revenue is falling, MR lies below AR. If average revenue is rising, MR lies above AR. When average revenue remain constant, AR=MR.

10. Draw the AR and MR curves under different markets.

Markets are broadly classified into two categories: perfectly competitive market and imperfectly competitive market. Accordingly revenue curves will be different for these two types of market.

AR and MR under perfectly competitive market

In perfect competition market the price is constant as the goods are homogeneous. So how the AR and MR remain unchanged when the output is increased that can we shown in following table.

Table 1

Output	Price	TR	AR	MR
1	10	10	10	10
2	10	20	10	10
3	10	30	10	10
4	10	40	10	10
5	10	50	10	10

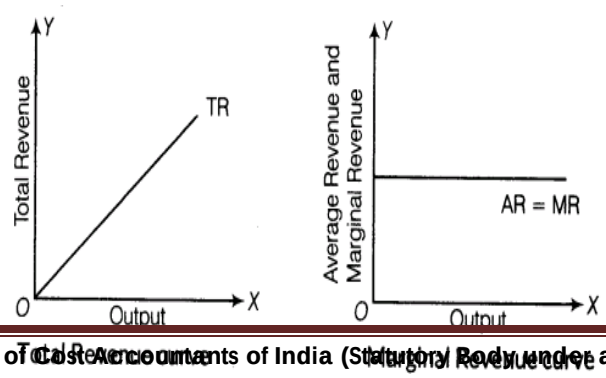


Figure: 8

Table 1 is represented by the figure 8. It is clear that total revenue will be a straight line through origin having a constant slope(which is the market price). Since P=AR=MR under perfect competition, so AR (=MR) curve will be a straight line parallel to the horizontal axis.

AR and MR under imperfectly competitive market

In imperfect market the price is changed. When the seller wants to increase the sales he must reduce the price. When the price is decreased, then the average revenue and marginal revenue are also decreased. This can be shown by the following schedule.

Output	Price	TR	AR	MR
1	10	10	10	10
2	9	18	9	8
3	8	24	8	6
4	7	28	7	5
5	6	30	6	2

From the above table AR and MR curves can be derived. This can be shown by the following diagram.

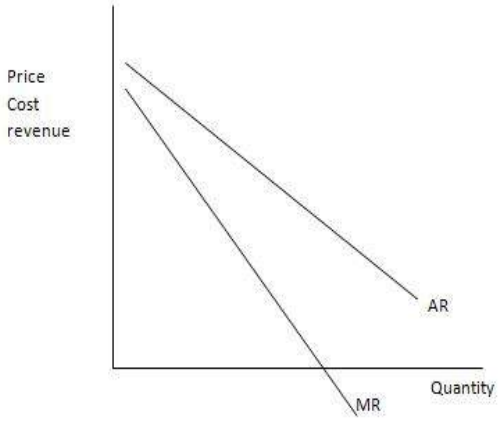


Figure: 9

From figure 9 it is clear that both AR and MR curves are falling and MR lies below AR. This is the feature of average and marginal revenue for an imperfectly competitive market.

SECTION – A : ECONOMICS
Study Note – 5
Market

Learning Objective:

The exchange of goods or services, with or without money, is a transaction. Market participants consist of all the buyers and sellers of a good who influence its price, which is a major topic of discussion in this Chapter.

I. Choose the correct answer

1. What is the shape of the demand curve of a firm under perfect competition?

(a) Negatively sloped

(b) Positively sloped

(c) Vertical

(d) Horizontal

2. The long run equilibrium condition of the firm under perfect competition is

(a) AR = MR = LAC =LMC =P

(b) AR = MR < LAC = LMC = P

(c) AR = MR > LAC = LMC > P

(d) AR < LAC = MR > LMC = P

3. Which one of the following conditions does not fit in the perfectly competitive market?

(a) Many sellers and many buyers

(b) Heterogeneous commodities

(c) Perfect knowledge

(d) Free entry and free exit

4. The necessary condition for profit maximisation of a competitive firm is

(a) P > MC

(b) P = AC

(c) P = MC

(d) P < MC

5. The MR curve of a competitive firm is
   (a) Vertical
   (b) Upward rising
   (c) U-shaped
   (d) Identical to AR curve

6. If P < SAC at the profit maximising level of output of a competitive firm, then the firm
   (a) Earns super normal profit
   (b) Earns only normal profit
   (c) Incurs loss
   (d) None of the above

7. A monopolist will suffer loss in the short run and will decide to stop production if
   (a) AR< AVC
   (b) AR = AVC
   (c) AC > AR > AVC
   (d) AR = AC

8. Perfect competition and monopolistic competition are having a common assumption. Find out which one of the following is the appropriate common assumption
   (a) The product is homogeneous
   (b) Perfect knowledge
   (c) Existence of selling cost
   (d) Free entry and free exit

9. Which one of the following oligopolistic model insists on co-operation?
   (a) Cournot's model
   (b) Bertrand model
   (c) Collusive oligopoly model
   (d) Edgeworth model

10. Assuming two markets where the price discriminating monopolist sells his product, the equilibrium condition in such a situation will be
   (a) MR1 = MR2 > MC
   (b) MR1 < MC > MR2
   (c) MR1 = MR2 = MC
   (d) MC = MR1 > MR2

Answer:

1. D,
2. A,
3. B,
4. C,
5. D,
6. C,
7. C,
8. D,
9. C,
10. C

II. Fill in the blanks:

1. **Firm under perfect competition is a price …….**
2. **Monopolist has ……. Supply curve**
3. **The other name of Monopolistic Competition is ……. …….**
4. **Doctor's service is an example of ……. …….**
5. **Kinked demand curve can be found in ……. Market**

Answer:

1. Taker
2. No
3. Product differentiation
4. Discriminating monopolist or, price discrimination
5. oligopolistic

III. True or False:

1. **At the profit maximizing output level of a monopolist, the marginal cost curve has to be upward rising.**
2. **Price discrimination will not be possible when the price elasticities of demand are the same in both the markets where the commodity is being traded by the discriminating monopolist.**
3. **The equilibrium level of output in the Cournot's model of duopoly is half of the competitive output.**
4. **A limit price is the price set by a monopolist to discourage economic entry in that market by keeping the limit price below the average cost.**
5. **Under perfect competition, the market price is determined by the interaction of the demand and supply forces in the market.**

Answer:

1. False,
2. True,
3. False,
4. True,
5. True

IV. Matching:

1. Dynamic pricing	**A. perceived demand curve**
2. Sticky price	**B. marginal cost pricing**
3. Monopolistic competition	**C. market economy**
4. Perfect competition	**D. internet**
5. P = MC	**E. oligopoly**

Answer:

1. D,
2. E,
3. A,
4. C.
5. B

V. Long answer type questions:

1. **What do you mean by a market? Explain the classification of the market.**
2. **How price is determined in a perfectly competitive market?**
3. **Describe the features of a monopolistic market.**
4. **Explain the characteristics of monopolistic competition.**
5. **How price and output are determined under oligopolistic market?**

Answer:

1. Market is a means by which exchange of goods and services takes place as the buyers and sellers interact with each other.

   Classification of the market

   On the basis of various criteria market can be classified into various types

(a) On the basis of area or locality

Market can be classified into three types. They are

1. Local markets
2. National markets
3. International markets

1. Local markets: sometimes a particular commodity is exchanged in the locality where it is produced. Then the commodity is said to have a local market. Vegetables, flowers, fruits may be produced and marketed in the same area.
2. National market: A commodity will have national market if it is demanded and supplied by people in different parts of the country. Commodities like wheat, sugar, coal, cotton have national market.
3. International market: If a commodity is sold and purchased in different countries, it is said to have international market, for example, gold, silver, wheat, garments, machine tools etc, have international market.

(b) On the basis of time element

Markets can be classified into three types

1. Very very short period market which is also called the immediate market. Perishable goods cannot be preserved for long period eg., fish market. Fish has to be sold immediately after catching it.

2. Short period market when we have certain fixed input, the amount of which cannot be changed during the time period. For example, rolling machine used in printing newspapers. This machine being very costly, the number of machine cannot be increased during a short period.

3. Long period market when all the inputs are variable inputs. This type of market is also very stable.

(c) On the basis of competition among the sellers or producers or firms

Markets can be classified into two types. They are

1. Perfectly competitive market
2. Imperfectly competitive market

Answer:

2. Price determination under perfectly competitive market:
Under perfect competition, the firm is the smallest producing unit and it has no influence on the market price. Firm is a mere price taker. In such a situation, market price is determined through the interaction of the demand and the supply force. Buyers and sellers are having opposing interests. If the price is low, the buyers will be interested in purchasing more. But the seller will be interested in selling more only when

the price is high. This is because price acts as an incentive to the seller. This indicates that demand and price are inversely related while supply is directly related to price. These two opposing forces – supply and demand will interact with each other and determine the equilibrium price which will clear the market. So in equilibrium, whatever has been demanded by the buyers will be supplied by the sellers. Or in other words, in equilibrium, supply is exactly equal to demand. A table will help us to understand the changes in supply and demand and the determination of the equilibrium price.

Price ($)	quantity demanded	quantity supplied
1	50	10
2	40	20
3	30	30
4	20	40
5	10	50

The table above shows the demand and supply schedule of the commodity. Changes in price are always causing a change in supply and demand. As price increases there is a fall in the quantity demanded. It means price and quantity demanded are inversely related. But a rise in price has increased the quantity supplied. Therefore, the relation between price and supply is direct. Every time a change in price is causing some change in the supply as well as demand. Only at price $3 it is observed that quantity supplied and quantity demanded are equal. So, $3 will be the equilibrium price.

Answer:

3. Features of Monopoly

The monopoly market has the following features:

1. **Single firm:** A single produces the commodity in the market. So there is only one seller or one producer or one firm.

2. **No close substitute :** A buyer in the monopolistic market has got no choice. Either she has to buy the product or go without it as there is no substitute for this product.

3. **Strong barriers to entry:** No new firm can enter this market due to certain restrictions in the market eg., huge investment, lack of technology, patents etc, prevent the new firm from entering.

4. **Firm and industry are identical:** As there is only one firm in monopoly market, there is no difference between firm and industry.

5. **Price maker:** the monopolist can determine the price of the commodity. So the monopolist is regarded as a price maker.

6. **Nature of AR & MR curves:** the average revenue curve and marginal revenue curve both slope downward to the right, because, when a seller wants to sell more of the product, he must reduce the price. When price is decreased, both AR & MR will be declining.

7. **Price discrimination:** the monopolist can charge different prices from different customers for the same commodity or service.

8. **Maximum profits:** the main aim of a monopolist is to earn maximum profit.

9. **Price and output determination:** In this market as there is only a single producer, he can control either the price or the supply of the commodity. But he cannot control both at the same time. He can increase the price by decreasing the output or, he can sell more output by decreasing the price. The sole objective of the monopolist is to maximize his profit. He will observe both the conditions for profit maximisation ie., MR = MC and MC curve must cut the MR curve from below.

Answer:

4. Monopolistic Competition Market:

The concept of monopolistic competition was introduced by Prof. Chamberlin. It is a market with many sellers for a product but the products are different in certain respects. The features of monopoly and competition are combined in this market. Hence, it is called monopolistic competition. Example: Cosmetics, Soaps etc.

Characteristics of Monopolistic Competition:

The main features are:

1. A considerable number of producers:

   A commodity is produced by a considerable number of producers. Since there are more number of producers no one controls the output in the market. Competition will be high among the producers.

2. Product differentiation:

   The commodity of each producer will be different from that of other producers. The difference may be due to material used, color design, smell, packaging, trademark etc. Because of this each product will have specific identification in the market.

3. Entry and exit:

   Firms are allowed to enter into production and leave the market. When profits are high new firms will join. In case of losses inefficient firms will leave.

4. Selling costs:

   An important feature of this market is every firm makes expenditure to sell more output. Advertisements through newspapers, journals, electronic media, sales representative, exhibitions, free sampling help to promote the sales. Lot of expenditure is made on these items under this market.

5. Imperfect Language:

   Buyers will have an imperfect knowledge about commodities. Sometimes products may be the same but consumers think that a particular good is superior than another. Due to the advertisements and other devices consumers purchase the commodities.

6. Price decision:

   Each firm produces a commodity with small differences. It is due to this reason that a firm will decide the price for its product

Answer:

5. Price and output determination under Oligopoly Market:

1. Cournot's Model:
   According to Cournot each duopolist believes that regardless of his actions and the effect upon the market of the product the other will go on producing the same commodity.
   Cournot output is two-third of the competitive output and the price is two- third of most profitable i.e. monopoly price.

2. Stackleberg Model:
   The producer under duopoly structure incorporates the decision level of his rival. It then incorporates in its own profit function and thereby maximize profit. Non-collusion is practiced at large. Leader-follower relation emerges.

3. Bertrand Model:
   According to this model each producer can always lower the price until price is equal to cost of production.

4. Edgeworth Model:
   Each duopolist believes that his rival will continue to charge the same price as he is just doing irrespective of what price he himself sets in. No determinate equilibrium can exist under duopoly.

5. Collusive Oligopoly:

   According to this model a cartel is formed when firms jointly fixes the price and output with a view to maximize joint profit.

   For Example: OPEC countries form a cartel.

   Pricing Strategies:

   Cost-plus pricing

   Cost plus pricing is the simplest pricing method. The firm calculates the cost of producing the product and adds on a percentage (profit) to that price to give the selling price.

   Limit pricing:

   A limit price is the price set by a monopolist to discourage economic entry in to a market. The limit price is often lower than the average cost of production of just low enough to make entering not profitable.

   Penetration pricing:

   Setting the price low in order to attract customers and gain market share. The price will be raised later once this market share is gained.

   Price leadership:

   An observation made of oligopolistic business behavior in which one company, usually the dominant competitor among several, leads the way in determining prices, the other's soon following.

SECTION – A : ECONOMICS
Study Note – 6
Money

Learning Objective:

Value of money is a term that is necessary to be understood to get acquainted with the theories of money. The velocity of circulation of cash depends on various factors, such as frequency of transactions, trade volume, type of business conditions, price levels, and borrowing and lending policies. However, in extreme conditions, an increase in the quantity of money would lead to a proportional decrease in the value of money, while keeping other factors at constant and vice versa; this Chapter throws light upon these.

I. Choose the correct answer:

1. Which one of the following is not the function of money?
- **(a) Medium of exchange**
- **(b) Measure of wealth**
- **(c) Standard of deferred payment**
- **(d) Store of value**

2. Which one of the following is the Fisher's equation?
- **(a) MP = VT**
- **(b) MT = VP**
- **(c) MV = PT**
- **(d) None of the above**

3. Which one of the following can not be the cause of the cost-push inflation?
- **(a) Wage increase not associated with rise in productivity**
- **(b) Rise in profit margin**
- **(c) High import price**
- **(d) Existence of excess demand**

4. In India money supply M1 is
- **(a) Currency + Demand deposits + Other deposits**
- **(b) Currency + Demand deposits + Term deposits**
- **(c) Currency + Demand deposits + Term borrowings**
- **(d) None of the above**

5. Which one of the following is not the primary function of money?
- **(a) Medium of exchange**
- **(b) Liquidity**
- **(c) Measure of value**
- **(d) None of the above**

6. Gresham's law states that
- **(a) Cheap credit drives away dear money**
- **(b) Metal money drives away paper money**
- **(c) Bad money drives away good money**
- **(d) None of the above**

7. The term inflation means
- **(a) Persistent rise in general price level over a long period**
- **(b) A rise in general price level over a long period**
- **(c) Value of money is rising**
- **(d) Rise in the rate of interest**

8. One of the demand-pull factors that creates inflation in India is
- **(a) Imposition of GST**
- **(b) Rising deficit finance of the Govt.**
- **(c) Hoarding of essential commodities**
- **(d) None of the above**

9. In Fisher's quantity theory, V is
- **(a) Value of money in circulation**
- **(b) Vertical movement of money**
- **(c) Velocity of money in circulation**
- **(d) None of the above**

10. In the Cambridge equation of the quantity theory, K stands for
- **(a) Cash balance**
- **(b) Capital stock**
- **(c) Current transaction**
- **(d) none of the above**

Answer:

1. B,
2. C,
3. D,
4. A,
5. B,
6. C,
7. A,
8. B,
9. C,
10. A

II. Fill in the blanks:

1. **Under the …….. system, the buyer must be willing to accept what the seller is willing to offer in exchange.**
2. **'Store of value' is the secondary function of ……..**
3. **In any country, currency is issued by the …….. …….**
4. **When aggregate demand exceeds aggregate supply, we have …… ……. Inflation.**
5. **According to …….. the rate of interest plays a dominant role in the determination of the value of money.**

Answer:

1. Barter,
2. Money,
3. Central Bank,
4. Demand pull,
5. Keynes

III. True or False:

1. **Lack of divisibility of commodities prevents barter system to work.**
2. **Measurement and distribution of national income is the primary function of money.**
3. **The one rupee note and coins are issued by the Finance Department of the Government of India.**
4. **Tax reduction will lead to fall in the rate of inflation.**
5. **There is a direct relationship between price level and value of money.**

Answer:

1. True,
2. False,
3. True,
4. False,
5. False

IV. Matching:

1. **Money**	**A. Bank cheque**
2. **Money supply**	**B. Velocity of money**
3. **Inflation**	**C. Currency**
4. **Fisher**	**D. Liquidity**
5. **Near money**	**E. Public spending**

Answer:

1. D,
2. C,
3. E,
4. B,
5. A

V. Long Answer type Questions:

1. **What are the difficulties faced by the barter system at the time of exchange of goods?**
2. **What are the functions of money?**
3. **Critically examine the quantity theory of money of Irving Fisher.**
4. **What are the causes of inflation?**

Answer:

1. Difficulties of the Barter system are as follows:

   (i) Lack of coincidence of wants

   (ii) Lack of store of value

   (iii) Lack of divisibility of commodities

   (iv) Lack of common measure of value

   (v) Difficulty in making deferred payments

   (i) Lack of coincidence of wants:

   Under the barter system the buyer must be willing to accept the commodity which the seller is willing to offer in exchange. The wants of both the buyer and the seller must coincide. This is called double coincidence of wants.

   (ii) Lack of store of value

   Some commodities are perishable. They perish within a short time. It was not possible to store the value of such commodities in their original form under the barter system. They should be exchanged before they actually perish. Otherwise, they would not be available for exchange when the need actually arises in future.

   (iii) Lack of divisibility of commodities

   Depending upon its quantity and value, it may become necessary to divide a commodity into small units and exchange one or more units for other commodity. But all commodities are not divisible. This is particularly true in the case of animals.

(iv) Lack of common measure of value

Under the barter system there was no common measure of value. To make exchange possible, it was necessary to determine the value of every commodity in terms of every other commodity.

(v) Difficulty in making deferred payments

Under barter system future payment for present transactions was not possible. For example, suppose a specific amount of rice is to be exchanged for a goat in view of the present value of the goat. The handing over of the goat can not be deferred to a future date because the value of the goat may change in future.

Answer:

2. Functions of Money:
Primary functions

A. Medium of exchange: Money serves as a medium of exchange. Money facilitates exchange of commodities without double coincidence of wants. People can exchange any good and service for money without any hindrance.
B. Measure of value: value of each commodity is expressed in the units of money. We call it a price. In view of this function of money, the values of different commodities can be compared and the ratio of their prices can be calculated easily.

Secondary functions

A. Store of value: Certain commodities are perishable. They can be exchanged for money before they perish. Thus their value can be preserved in the form of money.

B. Standard of deferred payments: In modern economies, most of the business transactions take place on the basis of credit. An individual consumer or a business man can purchase a commodity now and pay for it in future. Similarly, one can borrow money now and repay it in future with a premium.

C. Transfer of money: money can be transferred from one person to another at any time and at any place.

Contingent functions

A. Measurement s and distribution of national income: National income of any country can be measured in money by aggregating the value of all goods and services. Similarly, the national bread can be distributed among all the factors of production by making payments in terms of money.

B. Money equalises marginal utilities / productivities: Equi-marginal principal helps the consumer / producer maximise his satisfaction / profit. Money conducts the entire exercise of equating the marginal values in both the cases.

C. Basis of credit: Credit is created by banks from out of the primary deposits of money.

D. Liquidity: Money is the most important liquid asset. In terms of liquidity it is superior to all other assets. Money is 100% liquid.

Answer:

3. Quantity Theory of Money

Quantity Theory of Money:

1. Quantity theory by Irving Fisher:

The quantity theory of money explains about the value of money. Irving Fisher gave an equation to determine the value of money.

Irving Fisher used an equation [MV= PT]

MV = Money Supply

PT = Money Demand

Where, M = Money supply issued by the legal authority

V = Velocity of money

P = Price level

T = Total output

Fisher used the equation to show the relationship between money supply and price level as direct and proportional.

The rate of change in money supply (dm/m) is equal to rate of change in P (dp/p).

Main Points:

1. There is a direct or proportional relationship between money supply and price level.
2. There is an inverse relationship between money supply and value of money.
3. There is an inverse relationship between price level value of money.

Assumptions of Fisher equations:

1. (V) Velocity of money is constant
2. Gross national product (T) is also constant
3. This theory assumes money demand for transactional purpose only.

Criticisms:

1. Fisher's equation is abstract and mathematical truism. It does not explain the process by which M affects P.

2. It is presumed that entire M is used up in buying T instantly. It is unreal. No one spends all money the moment he earns it.
3. The concept of full employment is myth. There is a natural rate of unemployment in every country.
4. Even with full employment, a country can raise national output by bringing those factors which are not available within economy from abroad.
5. It is presumed that money is used for transactions only. Hence the theory is often referred to as cash transaction theory. This ignores the other roles of money.

Answer:

4. **Causes of Inflation**:

Primary Causes:

1. When demand for a commodity in the market exceeds its supply, the excess demand will push up the price ('demand-pull inflation').
2. When factor prices rise, costs of production rise ('Cost – push inflation')

   Let us now discuss in detail the various causes that may bring about inflation –

Increase in public spending:

1. Government's spending is important part of total spending in any modern economy.
2. It is an important determinant of aggregate demand.
3. In less developed economies, government expenditure has shown an upward trend.
4. This has created inflationary pressure on the economy.

Deficit financing of government spending:

1. Government spending increases beyond what can be financed by taxation.
2. In order to be able to incur the extra expenditure, the government resorts to deficit financing.
3. For instance, it prints money and spends it. This adds to the pressure of inflation.

Increased velocity of circulation:

1. Total use of money = money supply by the government x velocity of circulation of money.
2. In boom phase, people speed money at a faster rate.
3. The velocity of circulation of money is increases.

Population growth:

1. It is increase total demand in the market.
2. The pressure of excess demand will create inflation.

Hoarding:

1. Excess demand is sometimes artificially created by hoarders.
2. They stockpile commodities
3. They do not release them to the market.
4. This leads to excess demand and inflation.

Genuine Shortage:

1. If the factors of production are in short supply, production will be affected.
2. Supply will be less than demand, prices wil.l rise.

SECTION – B : ECONOMICS
Study Note – 7
Bank

Learning Objective:

Banks ***borrow from individuals, businesses, financial institutions, and governments with surplus funds called savings. Through the process of taking deposits, making loans, and responding to interest rate signals, the*** **banking** ***system helps channel funds from savers to borrowers in an efficient manner. This Chapter discusses functions of Banks and other financial institutions.***

I. Multiple Choice Questions:

1. Which one of the following is not a function of the commercial bank?
- **(a) Acceptance of deposits**
- **(b) Advancing of loans**
- **(c) Issuing of notes**
- **(d) Creating credit**

2. If the commercial banks get fresh deposits of Rs. 10 crores, assuming cash reserve ratio of 20%, they would be able to multiply deposits through loans and advances to the extent
- **(a) ₹ 20 crores**
- **(b) ₹ 200crores**
- **(c) ₹ 50 crores**
- **(d) ₹ 500 crores**

3. Which one of the following is not an instrument of monetary policy?
- **(a) Cash reserve ratio**
- **(b) Open market operation**
- **(c) Selective credit control**
- **(d) Indirect tax**

4. Which one of the following is the objective of the RBI?
- **(a) To maintain term deposits of the households**
- **(b) To ensure price stability**
- **(c) To arrange loans for the businessmen**
- **(d) None of the above**

5. In India, the Central Bank is nationalised and named RBI in the year
- **(a) 1947**
- **(b) 1948**
- **(c) 1949**
- **(d) 1950**

6. The basis of cash money issued by the RBI is
- **(a) Gold and foreign exchange reserve**
- **(b) The guarantee of the President of India**
- **(c) The guarantee of the Governor of the RBI**
- **(d) None of the above**

7. The full form of ATM of the commercial bank is
- **(a) All Time Money**
- **(b) Assured Transaction of Money**
- **(c) Automated Teller Machine**
- **(d) None of the above**

8. Which one of the following is not the function of the Central Bank?
- **(a) Credit control**
- **(b) Note issue**
- **(c) Act as banker's bank**
- **(d) Money creation**

9. If the cash reserve ratio is increased from 10% to 20%, how the credit creating power of the commercial banking system will be affected?
- **(a) Halved**
- **(b) Doubled**
- **(c) Increased by 10%**
- **(d) Decreased by 10%**

10. Cash Reserve Ratio is defined as
- **(a) Cash which the commercial banks have to keep with themselves.**
- **(b) Cash which a bank has to transfer to its branches.**
- **(c) Percentage of time and demand liabilities which a commercial bank has to keep in cash with the Central Bank**
- **(d) Ratio of credit to currency**

Answer:

1. (C),
2. (C),
3. (D),
4. (B),
5. (C),
6. (A),

7. (C),
8. (D),
9. (A),
10. (C)

II. Fill in the blanks:

1. **NABARD is the apex body in the …….. Credit.**
2. **Moral suasion is a ……..technique of credit control.**
3. **Whenever there is problem of liquidity, commercial banks approach the Central Bank for loan as the Central Bank is the Lender of the …… ……**
4. **UTI mobilize the savings of the relatively ……. Investors.**
5. **The headquarter of Asian Development Bank (ADB) is in …….. , Philippines.**

Answer:

1. Agricultural
2. Qualitative
3. Last Resort
4. Small
5. Manila

III. True or False:

1. **The main purpose of the SEBI is regulating business in stock markets and other securities market.**
2. **International Development Association (IDA) is affiliated to IMF.**
3. **EXIM Bank of India also provides business advisory technical assistance.**
4. **LIC was established in 1956 by nationalizing 100 private insurance companies.**
5. **IFCI was established to extend short term credit to the industrial units.**

Answer:

1. True
2. False
3. True
4. False
5. False

IV. Matching:

1. World Bank	**A. Principle of liquidity**
2. RBI	**B. SDR**
3. Commercial Bank	**C. Private Bank**
4. IMF	**D. Controller of credit**
5. ICICI	**E. IBRD**

Answer:

1. E,
2. D,
3. A,
4. B,
5. C

V. Long Answer Type Questions:

1. **What are the essentials of a sound banking system?**
2. **What are the credit control measures taken by the Central bank?**
3. **Distinguish between the central bank and the commercial bank.**
4. **Discuss the workings of the IMF.**

Answer: 1

Essentials of a sound Banking system:

A sound banking system promotes all round economic development of an economy. A good bank must have the following features:

(a) Adequate liquidity:

A bank must keep sufficient cash in hand to meet the claim of depositors, otherwise they would be insolvent. A bank failure not only affects depositors but banks also. People would not more keep funds with banker. It ensures safety of a bank. Unless a bank is safe it cannot render its social services.

(b) Expansion of banking:

Banking facilities should spread throughout the economy. It must also cover all sections of people in need of funds and all productive activities. The less- developed regions should get more banking facilities than others. Thus, diffusion of banking offices is essential.

(c) Investment and loan policies:

A sound banking system must have a sound investment policy whereby it can optimize the twin goals of liquidity and profitability. If loan and investments are wrong, a bank suffers loss or face liquidity shortage. A prudent banker should carefully determine the composition and character of its loans and advances so as to optimize earning without endangering safety and solvency.

(d) Human factor:

The soundness of a bank depends much on the quality of a banker. Banking being a practical affair, rigid application of bank laws are not always fruitful. Much depends on the discretion of men piloting the ship. Sound banking thus, depends more on banking personnel than on banking laws.

Answer: 2

Credit Control by Central Bank

A central bank possesses a number of instruments for controlling credit money.

These are of two types – Quantitative and Qualitative.

Quantitative techniques seek to regulate total quantity of credit while quantitative measures affect the availability of credit.

Bank Rate Policy:

As a banker's bank, a central bank lends money or rediscounts the bills of commercial banks.
The rate of interest charged by the central bank is known as Bank rate or Discount rate.
By manipulating bank rate central bank can regulate the credit creating power of member banks.
If bank rate is raised by the central bank, commercial banks are to borrow at a higher cost.
Then the y will increase their lending rate. This rate is known as the market rate.
The difference between market rate and bank rate is profit margin of commercial banks.
When bank rate rises market rate also rises and vice versa.
Demand for bank loan will reduce
On the other hand, for credit expansion, bank rate is reduced.
The effectiveness of this technique depends on the extent to which commercial banks depend on central bank for loan and rediscounting.
If banks can collect funds from other sources at relatively cheaper rate, they need not depend on central bank credit.
Again if investment opportunities are not present, the market demand for credit will weak, a fall in the bank rate may not raise the level of bank credit.

Open Market Operations:

It implies purchase and sale of securities in the stock market.
When the central bank appears in the market as a seller of government securities, people buy such securities by withdrawing money from banks or the banks themselves invest in such securities instead of granting loan to public.
In either case the powers of creating credit will be restricted.
On the other hand, if central bank buys securities money flows out thus enlarging the cash base of members banks.
Credit expansion depends upon external business environment and borrowers attitudes over which banks have no influence.

Variation or Reserve ratio:

Commercial banks are legally bound to keep a portion of their deposits in the form of cash reserve.
It is most liquid asset in their hand and at the same time it is zero earning assets.
Naturally by altering the CRR, the central bank can expand or reduce the funds bank can lend.
There exists an inverse relation between the size of cash reserve and the amount of credit given by a bank, assuming a given amount of deposit.
In under developed money market this technique is more suitable than open market operation or bank rate policy.

Qualitative Credit controls:

A central bank also possesses certain techniques by which it can control the direction and distribution of credit – purpose wise or areas wise.

The purpose of selective controls is the rational allocation of scarce bank credit and its economic utilization.

Further sectoral development of credit and controlling in other directions serve the purpose of preventing speculative activities with the help of bank finance and favoring productive activities.

These techniques are very helpful in a less-developed economy where overall credit restriction may hinder growth by preventing the flow of credit for investment.

Moral Suasion:

Moral suasion is a qualitative technique.

The central bank 'requests' banks to lend or not to lend in some sectors

There is no legal compulsion behind their acceptance.

Generally if a request is not carried out by the number bank, the guardian of the bank system may take such steps as banks are forced to accept.

The central bank is often empowered to issue directives to member banks.

Such direct orders are in the form of directional control, prohibiting loans of particular type of giving advice to grant loan to priority sectors.

Answer: 3

Distinction between the Central bank and Commercial bank:

Basis of Distinction	Central Banks	Commercial Banks
Monetary Authority	Enjoys supreme monetary authority with wide powers	No authority, hence no such power is enjoyed
Profit motive	It does not exist to make profits of its for owners	It exists and is organized for profits their owners.
Money supply to the economy	It is the ultimate source of money supply to the economy.	No such function is performed by it.
Services rendered	It acts as a banker to the government	It acts as a banker to private industrial and institutions
Chance of Failure	It is the lender of last resort and hence never fails	It often undertakes risky business activities and sometimes may fail
Service to the public	It neither does accept deposits from public, not lends money to public.	Accepting deposits and lending money to the public are the most important functions of commercial banks.
Ownership and managing authority	It is generally subordinate to the state, i.e. state owned and state managed.	It is mostly privately owned and privately managed.
Nature of operation	It issues paper notes in fact it enjoys the monopoly power in this matter.	Its nature operation is credit creation and cannot issue paper notes
Basis of operation	The basis of cash money issued is gold and foreign reserve.	The basis of credit money generated in cash deposit

Answer: 4

International Monetary Fund (IMF) – 1947

It was established in March 1947 one of the outcomes of Breton wood conference was IMF. The main object of IMF is to administer a code of fair practice in the sphere of foreign exchange and to make loans to the economies experiencing temporary deficit in their balance of payments.

Quota:

It is membership contribution fixed in terms of its national income and internal trade members are required to subscribe quota partly in gold (25%) party in domestic currency (75%).

Exchange rate:

Members of IMF had to declare the par value of national currency in terms of gold or American dollars. Once the par value of different currencies is fixed it becomes easy to determine the rate of exchange between two countries.

Special Drawing Rights (SDRs) – 1969:

SDR's was first introduced in 1969. It is the special currency issued by IMF. For two reasons IMF created SDR. They are

1. To overcome the shortage of gold in the world economy
2. To avoid the movement of gold across national boundaries.

SDRs are in coupons:

It is used in the place of gold. Hence it is called paper gold.

SECTION – B : ECONOMICS
Study Note – 8
Money Market

Learning Objective:

The *money market* plays a significant *role* in the *economy*. It serves as a *market* for indulging in transactions for a short period. The *Money market* does this by providing sufficient funds to trade as well as industry and which helps in implementation of monetary policies; are discussed in the Chapter.

I. Choose the correct answer:

1. Capital market deals with
- **(a) Short term credit**
- **(b) Liquid assets**
- **(c) Long term credit**
- **(d) Bills of exchange**

2. The unorganised Indian money market includes
- **(a) SBI**
- **(b) IDBI**
- **(c) Money lenders**
- **(d) LIC**

3. During peak season, the major drawback of the Indian money market is
- **(a) Seasonal stringency of credit**
- **(b) Higher interest rate**
- **(c) Both A and B**
- **(d) None of the above**

4. Multiplicity and disparity of interest rates exists in the Indian money market because
- **(a) There is credit immobility**
- **(b) There is wasteful competition between organised and unorganised sector**
- **(c) There is neck-to-neck competition within the organised and unorganised sector**
- **(d) Credit demand varies from region to region**

5. The rate at which funds are borrowed and lent in the call and notice money market is called
- **(a) Repo rate**
- **(b) Call money rate**
- **(c) Bank rate**
- **(d) Discount rate**

6. Commercial papers, as money market instruments, are issued by
- **(a) RBI**
- **(b) SBI**
- **(c) Highly rated corporate bodies**
- **(d) None of the above**

7. Non-resident Indian can also subscribe to Certificate of Deposit but only on a
- **(a) Non-repatriation basis**
- **(b) Non-profit basis**
- **(c) Non-negotiable basis**
- **(d) None of the above**

8. Treasury bills are
- **(a) Long term promissory notes**
- **(b) Medium term promissory notes**
- **(c) Short term promissory notes**
- **(d) None of the above**

9. In the Inter-bank Term Money Market, the participants are
- **(a) Commercial banks**
- **(b) Co-operative banks**
- **(c) Both A and B**
- **(d) Indigenous banks**

10. Commercial paper was introduced in the Indian money market on the recommendation of
- **(a) Milton Friedman**
- **(b) Lord John Maynerd Keynes**
- **(c) Marshall**
- **(d) Vaghul working group**

Answer:

1. (C),
2. (C),
3. (C),
4. (A),
5. (B),
6. (C),
7. (A),
8. (C),
9. (C),
10. (D)

II. Fill in The Blanks:

1. **The activities of the organised sector are systematically coordinated by the …….**
2. **Commercial papers are …….. promissory notes issued by corporate entries to raise resources.**
3. **In the commercial bill market, the bills of exchange are drawn by the …….. on the ……. for the value of goods sold.**
4. **The unorganised sector in the money market consists of …….. banks and money lenders.**
5. **Certificate of Deposits are deposit ……. issued by banks against deposits kept by individuals, companies, PSUs etc.**

Answer:

1. RBI
2. Unsecured
3. Seller, buyer
4. Indigenous
5. Receipts

III. True or False

1. **Money market is purely a market for short term funds or financial assets.**
2. **Money market is controlled and regulated by IDBI.**
3. **In call money market, funds are borrowed and lent for 14 days without any collateral security.**
4. **Commercial Paper represents a promise by the borrowing company to repay loan at a specified date.**
5. **In Inter-Bank Term Money Market, lenders can call back loan with a short notice.**

Answer:

1. True
2. False
3. False
4. True
5. False

IV. Matching:

1. Commercial Bill	**A. Notice Money Market**
2. Organised sector	**B. Treasury Bill**
3. Call Money Market	**C. unorganised sector**
4. Money Market Instrument	**D. Non-Scheduled Banks**
5. Money lender	**E. Liquid Asset**

Answer:

1. E,
2. D,
3. A,
4. B,
5. C

V. Long Answer Type Questions:

1. **Explain thenature of the money market.**
2. **What are the functions of Indian money market?**
3. **What are the defects of the Indian Money Market?**
4. **Suggest some measuresto improve the Indian money market.**

Answer: 1.

Money market is the nerve centre of the financial system. A well organised money market is the basis for an effective monetary policy. Money market mobilises savings from different sources and makes them available for investment. It is this mechanism through which funds flow from surplus units to deficit units in the economy.

Meaning of Money Market:
Financial markets are functionally classified into

A. Money market and
B. Capital market

This classification is on the basis of the term of credit, ie., whether the credit is supplied for a short period or long period. Money market refers to institutional arrangements which deal with short term funds. Capital market, on the other hand deals in long term funds. Money market is a short term credit market which deals with relatively liquid and quickly marketable assets such as: short term govt. securities, treasury bills, bills of exchange etc.

Objectives of Money Market:

A well developed money market serves the following objectives:

1. Provides an equilibrium mechanism for ironing out short term surplus and deficits.
2. Provides a focal point for the intervention of the central bank for influencing liquidity in the economy
3. Provides access to the user of short term money to meet their requirements at a reasonable price.

Characteristics of the Money Market:
Indian money market has the following major features:

1. Short term funds are borrowed and lent

2. No fixed place for conduct of operations. Transactions are conducted even over the phone.
3. Dealing may be conducted with or without the help of the brokers.
4. Short term financial assets that are dealt in are close substitutes of money
5. Funds are lent out for a maximum period of one year
6. Presence of a large number of sub-markets

Answer: 2.

Functions of Indian Money Market:

1. It links lenders and borrowers of short term funds. It is purely a market for short term funds or financial assets.
2. With agriculture
3. It provides financial assets with a high degree of liquidity e.g., call money, treasury bills, commercial bills etc.
4. It helps trade and commerce by developing a bill market and acceptance market
5. It enables the govt. to raise short term loans with treasury bill market.
6. It is controlled and regulated by RBI
7. It makes the monetary policy effective
8. It provides opportunities for lending the surplus funds of individuals, banks and other institutions.
9. It helps the central bank in maintaining stability of the value of the currency unit.

A well developed money market can perform the above functions effectively.

Answer: 3.

Defects of Indian Money Market

The Indian money market is inadequately developed, loosely organised and suffers from many weaknesses. Major defects are as follows:

1. Dichotomy between Organised and Unorganised sectors:
   Indian money market has two sectors (i) organised and (ii) unorganised. There is no coordination or cooperation between the two. So it is difficult for the Reserve Bank to ensure uniform and effective implementation of the monetary policy.

2. Predominance of Unorganised sector:
   The indigenous bankers which constitute a large portion of the unorganised money market remain outside the organised sector. Therefore, they seriously restrict the RBI control over the money market.

3. Wasteful Competition:
   Wasteful competition exists not only between the organised and un-organised sectors, but also among the members of the two sectors. The relation between various segments of the money market is not cordial. They are loosely connected with each other. Competition also exists between the Indian commercial banks and foreign banks.

4. Absence of All-India Money Market:
   Indian money market is not a single integrated all-India market. It is divided into small segments mostly catering to local financial needs. There is no link between money market in bigger cities like Mumbai, Chennai, Kolkata and those in smaller towns.

5. Inadequate Banking Facilities:
   After nationalisation of banks, there has been expansion of bank branches,but vast rural areas still exist without banking facilities. Compared to the size and population of the country, the banking facilities are not enough.

6. Shortage of Capital:
   The availability of capital in the money market is insufficient to meet the needs of industry, agriculture and trade.

7. Seasonal shortage of funds:
   A major drawback of the Indian money market is the seasonal stringency of credit and higher interest rate during peak period of the year. On the other hand, during slack season, from July to October the demand for credit and the rate of interest decline sharply.

8. Diversity of interest rates:
   Multiplicity and disparity of interest rates is another defect of the Indian money market. The interest rates also differ in various centres like Mumbai, Kolkata etc. Variations in the interest rate structure are largely because of the credit immobility. Costly and time consuming means of transferring money has created this problem.

9. Absence of Bill Market:
   The existence of a well organised bill market is essential for the proper and efficient working of money market. Short term bills form a much smaller proportion of the bank finance in India as compared to that in the advanced countries.

Answer: 4.

Measures to Improve Indian Money market:

1. The activities of the indigenous banks should be brought under the effective control of the RBI
2. Hundies used in the money market should be standardised and written in the uniform manner in order to develop an all-India money market.
3. Banking facilities should be expanded especially in the unbanked and neglected areas.
4. Discounting and rediscounting facilities should be expanded in a big way to develop the bill market in the country.
5. For raising the efficiency of the money market, the number of the clearing houses in the country should be increased and their working improved.
6. Adequate and less costly remittance facilities should be provided to the businessmen to increase the mobility of capital.

Variations in the interest rates should be reduced.

SECTION – B : MANAGEMENT
Study Note – 9
Management Process

Learning Objective:

Management process is a process of setting goals, planning and/or controlling the organizing and leading the execution of any type of activity, such as: a project or a process. An organization's senior management is responsible for carrying out its management process; are discussed in this Chapter.

I. Multiple Choice Questions:

1. Which is inherent in managerial job and embodied in all the functions of management?
- **(a) Planning**
- **(b) Organising**
- **(c) Control**
- **(d) Co-ordination**

2. _____ involves issuing orders to subordinates and supervises how these orders are carried out by them, and if necessary motivate the employees for higher performance.
- **(a) Supervision**
- **(b) Directing**
- **(c) Leading**
- **(d) None of the above**

3. Which of the following is the principle of direction?
- **(a) Harmony of objectives**
- **(b) Unity of Command**
- **(c) Follow up**
- **(d) All of the above**

4. Presence of _____ subordination inevitably brings chaos and disorder.
- **(a) Dual**
- **(b) Single**
- **(c) Both (a) and (b)**
- **(d) None**

5. A manager has to exhibit the style of leadership depending on the
   (a) Performance
   (b) Time
   (c) Situation
   (d) Period

6. _____ leads to higher job satisfaction.
   (a) Planning
   (b) Budgeting
   (c) Supervision
   (d) Motivation

7. The term communication is derived from the Latin word
   (a) Common
   (b) Communis
   (c) Communication
   (d) None

8. _____ is a bridge of meaning between two or more people.
   (a) Communication
   (b) Information
   (c) Planning
   (d) Reporting

9. The process of communication starts with
   (a) Supervisor
   (b) Sender
   (c) Receiver
   (d) None of the above

10. _____ is an essential to see that no distortion between the intended message and received message exists.
   (a) Medium
   (b) Encoding
   (c) Decoding
   (d) Feedback

11. When communication flows from top to bottom it is called _____
   (a) Horizontal communication
   (b) Upward communication
   (c) Downward communication
   (d) None of the above

12. When communication flows between various departments or people on the same level in an organization, it is called _____
    (a) Horizontal communication
    (b) Upward communication
    (c) Downward communication
    (d) None of the above

13. Tendency of people to interpret the same message in different ways may act as a _____ barrier.
    (a) Semantic
    (b) Emotions
    (c) Time pressure
    (d) Selective perception

14. _____ is concerned with providing the organization with the right number of people at the right place, and at the right time so that the organization would be able to achieve its goals effectively.
    (a) Recruitment
    (b) Staffing
    (c) Selection
    (d) Development

15. Manpower planning is also known as _____
    (a) Human Resource Accounting
    (b) Human Resource Management
    (c) Human Resource Planning
    (d) None of the above

16. Selection is a process of rejection and hence it is called a _____ process
    (a) Positive
    (b) Negative
    (c) Either (a) or (b)
    (d) None of the above

17. T-group training is also known as
    (a) Classroom Training
    (b) Apprenticeship Training
    (c) Internship Training
    (d) Sensitivity Training

18. _____ refers to the introduction of a person to the job and the organization.
    (a) Induction
    (b) Placement
    (c) Orientation
    (d) None of the above

19. The process of increasing the knowledge and skills of an employee for doing a particular job is known as
    (a) Training
    (b) Development
    (c) Education (d) None of the above

20. _____ refers to assigning rank and responsibility
    (a) Training
    (b) Development
    (c) Education
    (d) Placement

21. The process of choosing candidates who best meet the qualifications and requirements of the job is
    (a) Recruitment
    (b) Selection
    (c) Induction
    (d) Training

22. Which one is not the step in the staffing process?
    (a) Selection
    (b) Man power planning
    (c) Training and development
    (d) Education

23. Who contends that "Training is an act of increasing the knowledge and skill of an employee for doing a particular job"?
    (a) Edwin Flippo
    (b) Michael J. Jucius
    (c) O. Jeff Harris
    (d) Andrew Carnegie

24. The assignment of a specific person to act as either an instructor or resource person for the trainee is
    (a) Coaching
    (b) Apprenticeship training
    (c) Vestibule training
    (d) Job rotation

25. When an individual learns several different jobs within a work unit or department is known as
    (a) Coaching
    (b) Apprenticeship training
    (c) Vestibule training
    (d) Job rotation

26. Vestibule training is considered as a part of:
- **(a) Off-the-Job training**
- **(b) On-the-Job Training (c)**
- **(c) Both (a) and (b)**
- **(d) None of the above**

27. _____ without corresponding controls are apt to hollow hopes.
- **(a) Planning**
- **(b) Organising**
- **(c) Co-ordination**
- **(d) Directing**

28. Control system follows the following sequence:
- **(a) Establishment of standards – Measurement of actual performance – Comparing the actual performance with standards – Take corrective action.**
- **(b) Establishment of standards – Measurement of actual performance – Take corrective action – Comparing the actual performance with standards.**
- **(c) Establishment of standards – Comparing the actual performance with standards – Measurement of Actual performance – Take corrective actions – None of the above.**
- **(d) None of the above**

29. The first step in control process is
- **(a) Measurement of actual performance**
- **(b) Establishment of standards**
- **(c) Taking corrective action**
- **(d) Comparing the actual performance with standards**

30. The selected key areas for control are called
- **(a) Key result areas**
- **(b) Key success factors**
- **(c) Strategic points**
- **(d) All of the above**

31. ABC analysis is an example of
- **(a) Critical point control**
- **(b) Control by exception**
- **(c) Budgetary Control**
- **(d) Break Even Analysis**

32. Under ABC analysis, control attention is sought to be focused on ____ inventory items which are small in number but large in value.
- **(a) 'A' category**
- **(b) 'B' category**
- **(c) 'C' category**
- **(d) All of the above**

33. 'Control by exception' is also known as
    (a) Management by objectives
    (b) Management by exception
    (c) Critical point control
    (d) None of the above

34. According to 'Control by Exception', managers at each level should pay attention to only.
    (a) Exceptional deviations
    (b) Significant deviations
    (c) Exceptional and significant deviations
    (d) None of the above

35. Post control is also known as
    (a) Feedback control
    (b) Concurrent control
    (c) Pre-control
    (d) Feed Forward Control

36. Pre-control is also known as
    (a) Feedback control
    (b) Concurrent control
    (c) Post-control
    (d) feed forward control

37. Concurrent control is also known as
    (a) Post control
    (b) Pre-control
    (c) Real-Time control
    (d) Feed Forward control

38. Preventive control is also known as
    (a) Post control
    (b) Pre-control
    (c) Concurrent control
    (d) Steering control

39. The Thermostat in a refrigerator operates on the principle of
    (a) Steering control
    (b) Preventive control
    (c) Cybernetic control
    (d) Real Time control

40. Break-even analysis is also called as
    (a) Cost volume profit analysis
    (b) Ratio Analysis
    (c) Financial Analysis
    (d) None of the above

41. The process of dividing and subdividing up of duties and responsibilities which are necessary to any purpose and arranging them in groups which are assigned to individual is
    (a) Planning
    (b) Co-ordination
    (c) Organising
    (d) Staffing

42. The process that involves introduction of a new employee to the enterprise is
    (a) Orientation
    (b) Placement
    (c) Staffing
    (d) None of the above

43. The first step in the organizing process is
    (a) Division of work
    (b) Grouping the work
    (c) Identifying the work
    (d) Establishing Formal reporting relationships

44. ____ involves deciding in advance what is to be done, where, how and by whom it is to be done.
    (a) Organising
    (b) Decision making
    (c) Planning
    (d) None of the above

45. MBO is a concept introduced by
    (a) Henri Fayol
    (b) F.W. Taylor
    (c) Peter Drucker
    (d) George Terry

46. PERT stands for
    (a) Programme Evaluation and Review Technique
    (b) Planning Evaluation and Review Technique
    (c) Programme Evaluation and Review Theory
    (d) None of the above

47. CPM stands for
    (a) Critical Path Method
    (b) Critical Path Management
    (c) Control Path Method
    (d) Critical Planning Method

48. The basic assumptions about the environment in which plans are expected to be implemented is known as
    (a) Decision making
    (b) Forecasting
    (c) Planning premises
    (d) None of the above

49. The term strategy has a ___ origin.
    (a) Military
    (b) Air force
    (c) Navy
    (d) None of the above

50. Operational planning is also known as ---------- planning.
    (a) Corporate
    (b) Long range
    (c) Short-range
    (d) Strategic

51. The message to be transmitted through verbal medium may be
    (a) Orders
    (b) Instructions
    (c) Reports
    (d) All of the above

52. Which one is not a barrier to communication?
    (a) Filtering
    (b) Emotions
    (c) Message
    (d) Language

53. Feedback may be
    (a) Direct
    (b) Indirect
    (c) Either 'a' or 'b'
    (d) None of the above

54. Formal communication is always
- **(a) Written**
- **(b) Oral**
- **(c) Both 'a' and 'b'**
- **(d) None of the above**

55. _____ is concerned with providing the organization with the right number of people, at the right place and at the right time so that the organization would be able to achieve its goals effectively.
- **(a) Recruitment**
- **(b) Staffing**
- **(c) Selection**
- **(d) Development**

56. Which one of the following is the principle of direction?
- **(a) Harmony of objectives**
- **(b) Unity of command**
- **(c) Follow-up**
- **(d) All of the above**

57. _____ is aimed at maintaining harmony among employees and groups in an organisation
- **(a) Direction**
- **(b) Supervision**
- **(c) Planning**
- **(d) Control**

58. T-group training is also known as
- **(a) Classroom training**
- **(b) Apprenticeship Training**
- **(c) Internship training**
- **(d) Sensitivity training**

59. The process of communication starts with _____
- **(a) Supervisor**
- **(b) Sender**
- **(c) Receiver**
- **(d) Medium**

60. _____ refers to the introduction of a person to the job and the organization.
- **(a) Induction**
- **(b) Introduction**
- **(c) Orientation**
- **(d) Placement**

61. The first step in the organizing process is _____
    (a) Division of work
    (b) Grouping of work
    (c) Identifying the work
    (d) Establishing formal reporting relationships

62. Post control is also known as _____
    (a) Feedback control
    (b) Concurrent Control
    (c) Pre-control
    (d) Fast forward control

63. Control function is closely connected to _____
    (a) Planning
    (b) Organising
    (c) Coordination
    (d) All of the above

64. According to Mary Parker Follet which one is not the principle for achieving effective coordination?
    (a) Continuity
    (b) Early beginning
    (c) Self-coordination
    (d) Management Audit

65. Tendency of people to interpret the same message in different ways may act as a _____ barrier.
    (a) Semantic
    (b) Emotional
    (c) Language
    (d) Time

66. _____ involves the selection of language in which the message is to be given.
    (a) Medium
    (b) Decoding
    (c) Encoding
    (d) Feedback

67. Determination of the job to which an accepted candidate is to be assigned and his assignment to that job is called _____
    (a) Placement
    (b) Orientation
    (c) Induction
    (d) None of the above

68. _____ is the process which involves growth of an employee.
- (a) Training
- (b) Development
- (c) Education
- (d) All of the above

69. Manpower planning is also known as _____ .
- (a) Human Resource Accounting
- (b) Human Resource Planning
- (c) Manpower Management
- (d) All of the above

70. _____ refers to assigning rank and responsibility.
- (a) Training
- (b) Development
- (c) Education
- (d) Placement

71. _____ is vital for determining personnel needs of the organisation in future.
- (a) Recruitment
- (b) Staffing
- (c) Man-power planning
- (d) Development

72. When an individual learns several different jobs within a work unit or department it is known as
- (a) Coaching
- (b) Vestibule training
- (c) Apprenticeship training
- (d) Job rotation

73. The first step in control process is
- (a) Measurement of actual performance
- (b) Establishment of standards
- (c) Judging the action
- (d) Comparison of actual with standards

74. _____ without corresponding controls are apt to hollow hopes.
- (a) Planning
- (b) Organising
- (c) Staffing
- (d) Directing

75. Assignment of duties is meaningless unless adequate authority is given to _____.
    (a) Subordinates
    (b) Peers
    (c) Superiors
    (d) All of the above

76. Strategic decisions are made at ---------- level.
    (a) Middle
    (b) Lower
    (c) Top
    (d) all

77. The last, but not least important principle of direction is
    (a) Unity of command
    (b) Follow up
    (c) Direct supervision
    (d) Appropriate Leadership Style

78. Who contends that "Training is an act of increasing the knowledge and skill of an employee for doing a particular job"?
    (a) Edwin Flippo
    (b) Michael J. Jucius
    (c) O. Jeff Harris
    (d) Andrew Carnegie

79. MBO is a concept introduced by
    (a) Henri Fayol
    (b) F.W. Taylor
    (c) Peter Drucker
    (d) George Terry

80. _____ serve as bridges between activities and outcomes
    (a) Policies
    (b) Methods
    (c) Procedures
    (d) Rules

Answer.

1	d	26	a	51	d	76	c
2	b	27	a	52	c	77	b
3	d	28	a	53	c	78	a
4	a	29	b	54	a	79	c
5	c	30	d	55	b	80	c
6	d	31	a	56	d		
7	b	32	a	57	a		
8	a	33	b	58	d		
9	b	34	c	59	b		
10	d	35	a	60	a		
11	c	36	d	61	c		
12	a	37	c	62	a		
13	a	38	b	63	a		
14	b	39	c	64	d		
15	c	40	a	65	a		
16	b	41	c	66	c		
17	d	42	a	67	a		
18	a	43	c	68	b		
19	a	44	c	69	b		
20	d	45	c	70	d		
21	b	46	a	71	c		
22	d	47	a	72	d		
23	a	48	c	73	b		
24	a	49	a	74	a		
25	d	50	c	75	a		

II. Match the following:

1.

	Column I		**Column II**
1.	**Unity of Command**	**(A)**	**Steering control**
2.	**Break even analysis**	**(B)**	**One Superior and one subordinate**
3.	**Concurrent control**	**(C)**	**T – Group Training**
4.	**Sensitivity Training**	**(D)**	**Management by exception**
5.	**Control by exception**	**(E)**	**Cost Volume Profit**

Answer.

	Column I		Column II
1.	Unity of Command	(B)	One Superior and one subordinate
2.	Break even analysis	(E)	Cost Volume Profit
3.	Concurrent control	(A)	Steering control
4.	Sensitivity Training	(C)	T – Group Training
5.	Control by exception	(D)	Management by exception

2.

	Column I		**Column II**
1.	**Internal Sources**	**(A)**	**Assigning rank and responsibility**
2.	**External Sources**	**(B)**	**Transfer**
3.	**Training**	**(C)**	**Introduction of a person to a job**
4.	**Placement**	**(D)**	**Increasing the knowledge and skills of an employee**
5.	**Induction**	**(E)**	**Employment exchange**

Answer.

	Column I		Column II
1.	Internal Sources	(B)	Transfer
2.	External Sources	(E)	Employment exchange
3.	Training	(D)	Increasing the knowledge and skills of an employee
4.	Placement	(A)	Assigning rank and responsibility
5.	Induction	(C)	Introduction of a person to a job

3.

	Column I		**Column II**
1.	**Feature of Scientific Management**	**(A)**	**Max Weber**
2.	**Esprit de corps**	**(B)**	**Henri Fayol**
3.	**German Sociologist**	**(C)**	**Functional foremanship**
4.	**Father of Modern Management**	**(D)**	**Bureaucratic Management**
5.	**Rigid rules and regulations**	**(E)**	**Team work**

Answer.

	Column I		Column II
1.	Feature of Scientific Management	(C)	Functional foremanship
2.	Esprit de corps	(E)	Team work
3.	German Sociologist	(A)	Max Weber
4.	Father of Modern Management	(B)	Henri Fayol
5.	Rigid rules and regulations	(D)	Bureaucratic Management

4.

	Column I		**Column II**
1.	**Strategies**	**(A)**	**Investment Plans**
2.	**Determining Planning Premises**	**(B)**	**Step in Planning process**
3.	**Time Consuming**	**(C)**	**Limitation of Planning**
4.	**Controllable Premises**	**(D)**	**Single use plans**
5.	**Schedules**	**(E)**	**Standing Plans**

Answer.

	Column I		Column II
1.	Strategies	(E)	Standing Plans
2.	Determining Planning Premises	(B)	Step in Planning process
3.	Time Consuming	(C)	Limitation of Planning
4.	Controllable Premises	(A)	Investment Plans
5.	Schedules	(D)	Single use plans

5.

	Column I		**Column II**
1.	**Encoding**	**(A)**	**Oral communication**
2.	**Decoding**	**(B)**	**Channel of message transmission**
3.	**Group Discussions**	**(C)**	**Converting ideas into messages**
4.	**Filtering**	**(D)**	**Interpretation of the message**
5.	**Medium**	**(E)**	**Hiding some meaning**

Answer.

	Column I		Column II
1.	Encoding	(C)	Converting ideas into messages
2.	Decoding	(D)	Interpretation of the message
3.	Group Discussions	(A)	Oral communication
4.	Filtering	(E)	Hiding some meaning
5.	Medium	(B)	Channel of message transmission

6.

	Column I		**Column II**
1.	**Grapevine**	**(A)**	**Horizontal Communication**
2.	**Communication between peers**	**(B)**	**Element of Communication**
3.	**Communication with body movement**	**(C)**	**Informal Communication**
4.	**Communication from subordinate to superior**	**(D)**	**Upward Communication**
5.	**Message**	**(E)**	**Gestural Communication**

Answer.

	Column I		Column II
1.	Grapevine	(C)	Informal Communication
2.	Communication between peers	(A)	Horizontal Communication
3.	Communication with body movement	(E)	Gestural Communication
4.	Communication from subordinate to superior	(D)	Upward Communication
5.	Message	(B)	Element of Communication

7.

	Column I		**Column II**
1.	**Power to give orders and to ask for obedience**	**(A)**	**Scalar Chain**
2.	**Concentration of decision making authority at the top**	**(B)**	**Authority**
3.	**Proper hierarchy**	**(C)**	**Equity**
4.	**Systematic arrangement of things and people**	**(D)**	**Centralization**
5.	**Treating employees equally**	**(E)**	**Order**

Answer.

	Column I		Column II
1.	Power to give orders and to ask for obedience	(B)	Authority
2.	Concentration of decision making authority at the top	(D)	Centralization
3.	Proper hierarchy	(A)	Scalar Chain
4.	Systematic arrangement of things and people	(E)	Order
5.	Treating employees equally	(C)	Equity

III. State whether the following statements are True/False:

1. **Division of work is necessary to enjoy the benefits of specialization.**
2. **Apprenticeship training is best example for off the job training.**
3. **Decoding is said to be the carrier of message.**
4. **The first step in the process of organizing is identifying the work.**
5. **Rule of thumb is to be replaced by rule of science to improve the standards of performance.**
6. **Planning premises refer to the environment in which plans are to be implemented.**
7. **Communication is an exchange of facts, ideas, opinions or emotions by two or more persons.**
8. **Directing involves issuing orders to subordinates and supervises how these orders are carried out by them and if necessary, motivate the employees for higher performance.**
9. **A superior is always responsible to his subordinate.**
10. **Management can't be treated as "Exact Science" like chemistry or biology.**
11. **For every profession there are ethical codes fixed by professional associations which are binding on all the professionals.**
12. **According to Taylor, partial 'mental revolution' by way of change in the attitude and outlook of workers and management towards each other is absolutely essential to ensure harmony.**
13. **Unity of direction means that an individual employee should receive orders from one manager or superior.**
14. **Standing plans are used to attain a one-time goal.**
15. **Operational plans are developed by lower level management.**
16. **The term 'organization' refers to the relationship between people, work and resources used to achieve the common objectives.**
17. **Selection is the process of searching for prospective employees and stimulating them to apply for jobs in the organization.**
18. **A good system of control should work on the exception principle so that only significant deviations are brought to the attention of management.**
19. **Decoding is the process of converting ideas into messages.**
20. **Grapevine is informal communication.**
21. **Communication among peer groups is called upward communication.**
22. **Coordination is known as the essence of management.**

Answer.

1	True	12	False
2	False	13	False
3	False	14	False
4	True	15	True
5	True	16	True
6	True	17	False
7	True	18	True
8	True	19	False
9	False	20	True
10	True	21	False
11	True	22	True

IV. Long Answer type Questions:

1. Explain the meaning of 'Management'.

Answer.

Different authors have defined the term 'management' from different perspectives. Some of the important definitions given by eminent experts are presented below.

Mary Parker Follett defined management as the act of getting things done through people.

Frederick Taylor defined management as the art of knowing what you want to do in the best and cheapest way.

In the words of Henri Fayol, "To manage is to forecast and to plan, to organise, to command, to coordinate and to control".

According to Peter Drucker, "Management is a multi-purpose organ that manages business and manages managers and manages workers and work".

In the opinion of Harold Koontz, "Management is the art of getting things done through and with people in formally organized groups".

2. Discuss Management as a Science.

Answer.

The essential features of science are listed below.

(1) Systematic body of knowledge
(2) Cause & Effect Relationship
(3) Principles based on repeated experiments
(4) Principles derived on the basis of logical and scientific observations
(5) Universal Validity
(6) Replication is possible

Management has a systematic body of knowledge. It also establishes cause and effect relationship. For example, lack of parity (cause) between authority and responsibility will lead to ineffectiveness (effect). The various principles and concepts of management are the outcome of constant experimentation and observation. But management deals with human beings and human behaviour. As such, the experiments in the field of management are not always completely predictable or replicable. Management principles are not always based on logical and scientific observations because some kind of subjectivity enters in the observations due to presence of human element. The application and use of management principles is not always universal. These principles have to be modified according to the given situation. Replication is not possible in management. If' two managers are investigating same data, on different sets of human beings they will not get the same result because human beings never respond in exactly identical manner.

To sum up, management can't be treated as "Exact Science" like chemistry or biology (which deals with non-human entities) due to existence of human element. Human behaviour is indeed unpredictable. Individuals think, act or react differently under identical circumstances. Management is a social process. As such, it falls in the area of social sciences.

3. Discuss Management as an Art.

Answer.

The essential features of art are listed below.

(1) Systematic body of knowledge/Existence of theoretical knowledge
(2) Personalised application
(3) Practice and creativity
(4) Goal oriented
(5) Situational Application

The theoretical base may be same for each and every artist. However, each one has his/her own style and approach towards the job. That's why the success level and the performance quality differ from one artist to another. For example, there are quite a few qualified painters but M.F. Hussain is recognized for his style. Likewise, management, as an art, is also personalized. Every manager has his/her own way of managing things based on his/her knowledge, experience and personality. As a result, some managers

are known as good managers whereas others as not so good. It is known that practice makes a man perfect. Every artist becomes more and more skilful through regular practice. Similarly, managers learn through an art of trial and error initially. However, the application of management principles makes them perfect in the job of managing. Every artist has an element of creativity in line. That's why he/she aims at producing something new which requires combination of intelligence and imagination. Management is also creative in nature. It combines human and non-human resources in a useful way in order to achieve the desired results. Every art is result-oriented. Likewise, management is also directed towards accomplishment of pre-determined goals. The application of art varies from situation to situation. An art which is appreciated in one situation may not be appreciated in another situation. In management also, a particular management practice which is reasonably effective in an organization may not be effective in another organization because of change in situational context. Moreover, in the same organization, management practices may transform over the period of time because of change in contextual variables.

4. Discuss Management as a Profession in India.

Answer.

In order to understand whether management is a profession or not it is necessary to look at the characteristics of profession. A profession should have the following features:

(1) Well defined Body of knowledge
(2) Restricted Entry
(3) Presence of Professional Associations
(4) Existence of Ethical Codes
(5) Service Motive

Now, we have to see whether management has these characteristics or not. Management has a well defined systematised body of knowledge. The entry to a profession is restricted. For example, a person can practice as a Cost Accountant only when he is having degree from the Institute of Cost Accountants of India and has the certificate of practice from the same institute. In management, certificate of practice from the management institute is not mandatory. Anyone can become a manager irrespective of the educational qualification. However, many companies are now putting emphasis on appointing managers on the basis of professional qualification like MBA degree. Bar Council of India is there for lawyers, Medical Council of India is there for doctors, the Institute of Cost Accountants of India is there for the Cost Accountants. Before practising, membership of these associations is mandatory. In case of management, legally it is not compulsory for managers to become a member of the management associations like AIMA in New Delhi, National Institute of Personal Management at Calcutta etc. For every profession there are ethical codes fixed by professional associations which are binding on all the professionals. In case of management, All India Management Association (AIMA) has devised a code of conduct for Indian managers. But legally it is not compulsory for all the managers to get registered with AIMA and abide by the ethical codes. The basic motive of every profession is to serve the clients with dedication, whereas the basic purpose of management is the achievement of organisational objectives. To sum up, management is not an outright profession in India. But it is taking giant strides in that direction.

5. Explain the principles of Scientific Management.

Answer.

Principles of scientific management propounded by the eminent management expert F. W. Taylor are listed below.

(1) Science, Not Rule of Thumb: There should be no scope for trial and error in taking decisions. Rule of Thumb implies arriving at decisions on the basis of personal judgement or intuition. According to Taylor, every decision should be based on scientific enquiry with cause and effect relationships.

(2) Harmony, Not Discord / Conflict: Taylor put emphasis on cordial relationship between the workers and the management. Absence of harmony between the workers and the management will lead to conflict between the two which may result in undesirable consequences. According to Taylor, complete 'mental revolution' by way of change in the attitude and outlook of workers and management towards each other is absolutely essential to ensure harmony. Division of work, training, team spirit, positive attitude, sharing a part of surplus with workers etc. can reduce conflict and ensure harmony.

(3) Cooperation, Not Individualism: It is the extension of the harmony principle. It can be ensured through categorical division of labour. Here, the emphasis is on mutual cooperation between the workers and the management. It is important that the management should always guide, encourage and help the workers. A sense of individualism can lead to diversion from the unified goals, ultimately affecting the prospect of the entire organization.

(4) Maximum not Restricted Output: Maximum output will result in higher wages for the workers and greater profit for the management. Increased productivity is beneficial for the society at large. Both the management and workers should attempt to accomplish maximum output in place of restricted output. This will be beneficial to both the parties.

(6) Scientific Selection, Training and Development of Workers: There should be scientifically designed procedure for the selection of workers. Physical, mental & other requirement should be specified for each and every job. According to Taylor efforts should be made to develop each employee to his greatest level and efficiency & prosperity.

6. Discuss the criticisms levelled against Scientific Management.

Answer.

The important criticisms levelled against Scientific Management are listed below.

a) In the opinion of some experts, human element is ignored. The principles of scientific management will make the workers mechanical and robot. Over-specialisation and repetition of jobs under scientific management makes them monotonous.

b) Too much importance is given on individual performance and not on group performance.

c) Some experts argue that the workers are exploited because wages do not rise in proportion to rise in production.

d) Weakening of trade unions is also a serious objection on the part of the labour unions. There are no rooms for trade unions to bargain as everything is standardized.

e) It is expensive and time consuming.

f) It may result in loss of initiative for skilful workers.

g) There may be difficulties in getting trained personnel.

h) There is absence of non-monetary incentives such as job security, praise, workers participation in management, social recognitions.

i) It is very difficult to develop 'One Best Way' of work.

j) It is really difficult for the small firms to comply with the requisites of Scientific Management.

k) According to Peter F Drucker, because of the separation of planning from doing, administrative policies cannot be well-planned.

7. Explain Henri Fayol's 14 principles of Management.

Answer.

(i) **Division of work:** According to Henri Fayol, specialization promotes efficiency of the workforce and increases productivity. In addition, the specialization of the workforce increases their accuracy and speed.

(ii) **Authority and Responsibility:** According to Fayol, authority is the right to give orders to the subordinates. The responsibility can be traced back from performance. In other words, authority and responsibility go together and they are two sides of the same coin. The result of authority is responsibility.

(iii) **Discipline:** The individuals working in the organization must be well-disciplined. The discipline refers to the obedience, observance of established rules and respect for authority.

(iv) **Unity of Command:** It means that an individual employee should receive orders from one manager or superior and that the employee is answerable to that manager or superior. If tasks are given to an employee by more than one manager or superior, this may lead to confusion which may lead to possible conflicts for employees.

(v) **Unity of direction:** According to Fayol, each group of activities having the same objectives must have one head and one plan. In the opinion of Fayol, for the efficient running of an organisation the unity of direction is important, while the unity of command is important to enhance the efficiency of the employees.

(vi) **Subordination of individual interest to general interest:** For ensuring smooth functioning of the organization, Fayol opined that personal interests are subordinate to the interests of the organization. The primary focus should on the accomplishment of organizational objectives and not on achieving the individual objectives.

(vii) **Remuneration: According to this principle,** the remuneration should be sufficient to keep employees motivated and productive.

(viii) **Centralization:** In centralization, the authority is concentrated only in a few hands. However, in decentralization, the authority is distributed to all the levels of management. No organization can be completely centralized or decentralized. As a result, there should be a balance between centralization and decentralization.

(ix) **Scalar chain:** Henri Fayol talked about a clear line of hierarchy from the top rung to the lowest so that every employee knows who his immediate senior is in the times of conflict or crisis. It suggests that each individual must know from whom he shall get instructions and to whom he is accountable to.

(x) **Order:** This principle is concerned with the systematic arrangement of things and people in the organization. It implies that every material should be in its place, and there should be a place for every material. Likewise, in the case of people, a right man should be in the right job. According to Fayol, every enterprise should have two different orders- Material Order for Physical Resources and Social Order for Human Resources.

(xi) **Equity:** According to Henri Fayol, all the employees in the organization must be treated equally with respect to the justice and kindliness.

(xii) **Stability of tenure of personnel:** According to this principle, employee should have stability of tenure and should be given sufficient time to show their performance. Moreover, frequent transfers or rotations should also be avoided. Fayol believed that instability in the tenure of employees is a cause of poor management and results. High rate of labour turnover will result in increased expenses because of selecting them time and again, and giving them training afresh. It also lowers the prestige of the organisation.

(xiii) **Initiative:** According to Fayol, it is the duty of the manager to encourage the feeling of initiative among his employees for doing some work or taking some decision but within the limits of authority and discipline. It will be possible only when the manager will welcome the thoughts of his/her subordinates. By doing so the subordinates will present new and useful ideas time and again and gradually they will become an integral part of the organisation. It develops sense of belongingness in employees.

(xiv) **Esprit de Corps:** This principle implies that union is strength. Fayol emphasized on the need for teamwork. This means "unity is strength". The feeling of 'I' should be replaced with 'We' in the managers while having a conversation with the workers. It helps to develop an atmosphere of mutual trust and understanding.

8. Define Planning. Explain the Characteristics / features of Planning.

Answer.

Definition of Planning

Planning is an intellectual process. Planning is thinking before doing. It bridges the gap between where we are and where we want to go.

Planning is deciding in advance what to do, how to do, when to do and who is to do it (Koontz & O'Donnell).

Characteristics / features of Planning

(i) **First and foremost managerial function**: Planning is the first function in the process of management. According to Koontz, planning provides the basic foundation from which all future management functions arise.

(ii) **Futuristic**: Planning is concerned with future. It is the process of coping with future uncertainties.

(iii) **Goal oriented**: It is concerned with the establishment of objectives or goals of the organization. Every plan specifies the objectives to be attained in future and steps necessary to reach them.

(iv) **Continuous Process**: It is a continuous and integrated process. It is an ongoing process as the plans are framed, executed and followed by another plan.

(v) **Decision making**: Planning involves decision-making. Planning essentially involves choice among various alternative courses of action. If there is one way of doing something, there is no need for planning.

(vi) **Intellectual Process**: Planning is an intellectual process involving mental exercise. It involves creative thinking and imagination. Planning compels managers to abandon guesswork and wishful thinking. It makes them think in a logical and systematic manner.

(vii) **Pervasive**: It is pervasive. It is present in all the segments and is required at all the levels of the organisation.

(viii) **Flexibility:** Planning is based on a forecast of future events. Since future is uncertain, plans should be reasonably flexible. When market conditions change, planners have to make necessary changes in the existing plans.

9. What are the limitations of Planning?

Answer.

The limitations of planning are listed below.

(i) Success not guaranteed: Planning does not guarantee success.

(ii) Unsuitable for emergencies: Planning cannot face sudden emergencies. Planning requires too much of time and the decision-making process may get delayed. Time is a serious limitation where prompt actions are required.

(iii) Rigidity: Planning creates rigidity. There may be internal and external inflexibility.

(iv) Resistance to change: Resistance to change on the part of the employees is a serious limitation of planning. Such resistance comes because of the thinking that the present plan is better than the proposed plan.

(v) External limitations: Planning is effected by external limitations. It is affected by certain factors which are not within the control of the planners. These factors are political, social, economical and technological.

(vi) Reduces Creativity: According to Terry, "Planning strangulates the initiative of the employees and compels them to work in an inflexible manner."

(vii) Cost: Planning involves huge costs.

10. What are the steps in Planning Process?

Answer.

The steps in the planning process are listed below.

(i) Establishing Objectives:
Establishing the objectives is the first step in planning. Plans are prepared with a view to achieving certain objectives or goals of the organization. Accordingly, plans should reflect objectives of the organization. Plan must ensure that every activity undertaken contributes to the achievement of objectives.

(ii) Determining Planning Premises:
Planning premise is planning assumptions about the expected environmental and internal conditions. Such premises may be external and internal. External premises include total factors in task environment like political, social, technological, competitors' plans and actions, government policies, etc. Internal factors include organization's policies, resources of various types, and the ability of the organization to withstand the environmental pressure. The plans are formulated in the light of both external and internal factors. Forecasting plays a major role in planning premises.

(iii) Determining Alternative Courses:

There are a number of ways of doing a thing. The planner should study all the alternatives very carefully. According to Koontz and O'Donnell, "There is seldom a plan made for which reasonable alternatives do not exist." All the pros and cons of methods should be weighed before a final selection.

(iv) Evaluating Alternative Courses:

Evaluation can be difficult because of uncertainty about the future, various intangible factors and inaccurate premises behind plans. Evaluation can be difficult because of uncertainty about the future, various intangible factors and inaccurate premises behind plans. Several techniques can be used by managers at this step. In fact, it is at this step in the planning process that operations research and mathematical as well as computing techniques can be primarily applied.

(v) Selecting the Best Course:

After having evaluated the various alternatives, the most suitable alternative is selected. It is exactly the point at which decisions are made.

(vi) Formulating Derivative Plans:

The main plan should be supported by a number of derivative plans. Within the framework of a basic plan, derivative plans are formulated in each functional area. Segregation of master plan into departmental, sectional and individual plans helps in understanding the real nature of future uncertainties.

(vii) Implementation of Plans:

It is the final step in the process of planning. This involves putting the plans into action so as to achieve the objectives of the organization.

(viii) Reviewing the Plan – Reviewing the plan help managers to evaluate the effectiveness of the plan. A system of thorough review and scrutiny can help in detecting derivations from the set plans and remedial measures can be taken accordingly.

11. Explain the different types of plans.

Answer.

Different types of plans are presented below in tabular form.

On the basis of use	On the basis of time	On the basis of managerial level:	On the basis of Nature
Single Plan	Long Term Plan	Top level Plans	Operational Plan
Standing Plan	Intermediate Plan	Middle-level Plans	Tactical Plan
	Short-term Plan	Lower level Plans	Strategic Plan

Single Plan: Such plans are used to attain a one-time goal. These plans address unique events which are not going to happen frequently. In other words, the aim of such plans is to meet the needs of a particular situation. Computerization process in banking industries is an example of such plan. Plans formulated for acquisition or merger process is another example.

Standing Plan: Such plans are used to handle events which happen frequently. These plans are also known as 'multi-use plans'. Such plans offer guidance for those actions of the organization which are repetitive in nature. These plans result in considerable saving in time.

Long Term Plan: Such plans are made by the top level management. These plans are strategic in nature. These plans have influence on the entire organization. The range of such plans usually varies between 1 year and 10 years.

Intermediate Plan: Such plans are made by the middle level managers. These plans influence the respective departments of the organization. The range of such plans usually varies between 6 months and 1 year.

Short-term Plan: Such plans are made by the lower level managers. These plans influence the day-to-day operations of the organization. The range of such plans usually varies between 1 week and 1 year.

Top level Plans: Such plans are made at the top level of management.

Middle-level Plans: Such plans are made at the middle level of management.

Lower level Plans: Such plans are made at the lower level of management.

Operational Plan: Such plans are developed by lower level management. These plans are short-term plans. These plans affect only specific departments of the organization. The level of uncertainty is relatively low since these plans are meant for short term.

Tactical Plan: Such plans are developed by middle level management. The duration of such plans may be short-term or medium term. These plans affect the functional areas of the organization like marketing, manufacturing, financing, human resource etc. The scope of such plans is broader than operational plans but narrower than strategic plans.

Strategic Plan: Such plans are developed by top level management. These plans are long-term plans. These plans affect the entire organization in a significant manner. The level of uncertainty is high since these plans are meant for long term.

12. Explain the pre-requisites of effective planning in an organization.

Answer.

The pre-requisites of an effective planning in an organization are listed below.

(i) Top Management Support: Planning should start from the top. According to Koontz, O'Donnell and Weihrich, "the example and drive of top managers are the most important single force in planning".

(ii) **Involvement of subordinates:** There should be wide and spontaneous participation in planning by the subordinates from the very formulation stage.

(iii) **Proper assessment of resources:** The resources available within the organisation should be properly assessed while making a plan.

(iv) **Awareness and acceptance of change:** According to Koontz, O'Donnell and Weihrich, "it must be an objective of managers to build in their organizations an awareness of change, an ability to forecast in and a welcoming attitude towards it".

(v) **Setting up a monitoring system:** Regular appraisal and review of plans is absolutely essential. Every plan should be refined and restructured on the basis of accurate and timely information.

(vi) **Fit the plan to the situation:** These days planning has become situational. A change in any part of the environment must be sensed and appropriate strategy must be determined to cope with the change.

13. What is meant by planning premises? Explain the different types of planning premises.

Answer.

Planning premises

Planning premises means systemic and logical estimate for the future factors affecting planning.

In the words of G.R. Terry, "planning premise are the assumptions providing a background against which the estimated events affecting the planning will take place". In order to make the plans more operational and realistic, these assumptions are necessary.

Different types of planning premises

Different types of planning premises are:

(a) **Internal and External premises:** Internal premises come from the organization itself. These include sales forecast, management philosophy, skills of the workers etc. On the other hand, external premises come from external environment. Cultural, economic, political, social and technological environments constitute external environment. External premises can't be controlled by the organization.

(b) Controllable, Semi-controllable and Non-controllable premises: Premises which can be controlled by the management are known as controllable premises. Factors like materials, money and machines are areas where management has maximum control. Semi-controllable premises are under the partial control of a business. Examples of such premises are demand for the product, Trade union relations. Non-controllable premises are totally beyond the scope of business like government policy, international trade agreements, wars, natural calamities etc.

(c) Tangible and Intangible premises: Premises which can be measured quantitatively are known as tangible premises. They may be quantified in terms of money, time and units of production. Premises which cannot be measured quantitatively are known as intangible premises. Examples include reputation of the business, public relations, employee morale etc.

Different types of premises tend to overlap each other. For instance, internal premises may also be controllable (organisational policies) and tangible premises (cost of product), external premises can also be non-controllable premises (economic policies). External premises can also be tangible (rate of inflation) or intangible (value system of the society).

14. Define Organisation. Explain organization as a process.

Answer.

Definition of 'Organisation'

The term 'organization' refers to the relationship between people, work and resources used to achieve the common objectives (goals). It follows planning. It is a function in which the synchronization and combination of human, physical and financial resources takes place. It is the process of assigning tasks and allocating resources to individuals to enable them to accomplish organizational goals. In essence, organizing is the managerial function that deals with the allotment of duties, co-ordination of tasks, delegation of authority, sharing of responsibility etc.

Process / Steps of Organisation

The steps involved in the process of organization are listed below.

(i) Determining the work activities necessary to accomplish objectives: The first step in the organizing process is to identify the work to be performed in the organisation. Every organisation is created to achieve some predetermined objectives. It is absolutely essential to identify the work to be performed to achieve those objectives.

(ii) Classifying and grouping activities: Dividing work is the essence of organizing function. After making the vision, similar activities shall be grouped together in order to provide for a smooth flow of work. Departments and divisions are created in an organisation based on the principle of similarity and relatedness of the activities performed. These departments or divisions are then managed under the direction of an individual called manager of the particular department.

(iii) Assigning work / duties and delegating appropriate authority: Authority is the right to act and extract obedience from others. A manager may not be able to perform tasks without granting authority to him by the organisation. While assigning duties the manager should clearly specify authority and responsibility limits.

(iv) **Designing a hierarchy of relationships / establishing reporting relationship:** Establishment of formal reporting system should pave way for assigning the duties and responsibilities to individual in an unambiguous fashion.

15. What is meant by Staffing? Explain the importance of Staffing.

Answer.

Meaning of 'Staffing'

Staffing is the process of recruitment, selection, development, training and compensation of the managerial personnel. In a newly created enterprise, the staffing would come as a. third step—next to planning and organizing—but in a going enterprise the staffing process is continuous. McFarland defined staffing as the function by which managers build an organization through the recruitment, selection, and development of individuals as capable employees.

Importance of Staffing

The importance of staffing is stated below.

(i) **Human element:** It puts emphasis on human element.

(ii) **Motivation:** It leads to motivation to work.

(iii) **Increased efficiency:** It results in increase in efficiency of the workers.

(iv) **Competitive advantage:** It gives the organization a competitive advantage.

(v) **Potential managers:** It aids in developing potential managers.

(vi) **Facilitating control:** It facilitates control.

(vii) **Optimum resource utilization:** It ensures optimum utilization of human resources.

(viii) **High morale:** It helps in building higher morale.

(ix) **Increased productivity:** It leads for maximum productivity and higher performance.

(x) **Cost reduction:** It reduces the cost of manpower by eliminating the wastage of the human resources.

(xi) **Organisational growth:** It provides for the development of the employees and through them it ensures continuous survival and growth of the organization.

16. Explain the steps in the Staffing process.

Answer.

The steps in the Staffing process are listed below.

(i) **Manpower Planning:** It is an estimation of manpower requirement. Here, the objective is not only to find out number of people needed but also the type of people. It can be regarded as the quantitative and qualitative measurement of work force required in an organization.

(ii) **Recruitment:** It is the process of searching for prospective employees and stimulating them to apply for jobs in the organization. It may be internal (transfers and promotion) and external (placement consultants, employment exchanges, contractors, advertisement).

(iii) **Selection:** It is the process of eliminating those who appear unpromising. The selection is done through a process, which involves test, interviews, etc.

(iv) **Placement and Orientation:** Placement is the process of putting the person on the job for which he is selected. Orientation is the process of familiarizing the new employees with the existing.

(v) **Training and Development:** Training is the process of enhancing the knowledge and skills of an employee. It is a job-oriented process. On the other hand, development is the process of learning and growth. It is a career-oriented process.

17. What is meant by Recruitment? Explain the different sources of Recruitment.

Answer.

In the words of Edwin Flippo, 'recruitment is the process of searching for prospective employees and stimulating them to apply for jobs in the organisation'. It is the process of bringing together those who are offering jobs and those who are seeking jobs. Recruitment is a positive process where a pool of prospective employees is created and management select the right person for the right job from this pool. It provides a base for the selection process.

Different sources of Recruitment

Recruitment may be internal (transfers and promotion) and external (placement consultants, employment exchanges, contractors, advertisement).

Internal Sources of Recruitment

1. **Promotions:** Promotion results in enhancements in pay, position, responsibility and authority.A promotion from within policy can stimulate great motivation among employee. This in turn can result in improvement in the employee morale.
2. **Retirements:** The retired employees may be given the extension in their service in case of non-availability of suitable candidates for the post.
3. **Former employees:** Former employees who had performed well during their tenure may be called back, and higher wages and incentives can be paid to them.
4. **Transfer:** Employees may be transferred from one department to another wherever the post becomes vacant. There is usually no drastic change in the pay or status of the employees.
5. **Internal advertisement:** The existing employees may be interested in taking up the vacant jobs. Since they are working in the company for long time they know about the specification and description of the vacant job. For their benefit, the advertisement within the company is circulated so that the employees will be intimated.

External Sources of Recruitment

1. **Press advertisement:** A wide choice for selecting the appropriate candidate for the post is available through this source. It gives publicity to the vacant posts and the details about the job in the form of job description and job specification are made available to public in general.
2. **Campus interviews:** It is the best possible method for companies to select students from various educational institutions. It is easy and economical. The company officials personally visit various institutes and select students eligible for a particular post through interviews.
3. **Placement agencies:** A databank of candidates is sent to organizations for their selection purpose and agencies get commission in return.
4. **Employment exchange:** People register themselves with government employment exchanges with their personal details. According to the needs and request of the organization, the candidates are sent for interviews.
5. **Walk-in-interviews:** These interviews are declared by the organizations on the specific day and time and conducted for selection.
6. **E-recruitment:** Various sites such as jobs.com, naukri.com, and monster.com are the available electronic sites on which candidates upload their resume and seek the jobs.
7. **Competitors:** By offering better terms and conditions of service, the human resource managers try to get the employees working in the competitor's organization.

18. Define Selection. Explain the process of selecting the candidates for employment in an organization.

Answer.

Definition of 'Selection'

It is the process of eliminating those who appear unpromising. Selection is done through a process, which involves test, interviews, etc. The procedure of selection may vary from industry to industry, company to company and even from department to department.

Process of selecting the candidates for employment in an organization

The main steps in the process of selection are described below.

1. **Preliminary interview:** Here, totally unsuitable applicant is eliminated. The candidates who pass this step are only asked to fill in the application form. It results in cost saving.

2. **Receiving applications:** On clearing the preliminary interview the candidate is asked to fill in the standard application form which contains information about the age, qualification, experience etc. It gives the interviewer an idea about the candidate and such information also helps in formulating questions.

3. **Screening of applications:** The next step is the screening of applications received from the applicants. Candidates who qualify the criteria of the screening committee are called for the interview. Interview letter is sent to them.

4. **Employment test:** These tests are done to check the ability of the candidate. Such tests vary from organization to organization and change as per the need of the particular job. These tests are intelligence tests, aptitude tests, trade tests, interest test, personality tests etc.

5. **Employment interview: C**andidates qualifying the above tests are called for the employment interview. This interview is done (a) to get more information about the candidate, (b) to give him the actual picture of what is required from him, and (c) to check the communication skill of the candidate for senior position post. A panel is prepared for taking the interview. On completion of interview of each candidate, the members of panel give the grades. There may be direct interview or indirect interview.

6. **Checking references:** The person who gives the reference of a potential employee is an important source of information. The referee can provide information about the person's capabilities, experience in the previous companies and leadership and managerial skills. The information provided by the referee is to be kept confidentially.

7. **Physical examination:** The organizations generally prefer medical examination to avoid time and expenditure spend on the medically unfit person.

8. **Final selection:** Finally, letter of appointment is issued to the candidate. Initially he is appointed on probation basis for certain period of time. On successful completion of probationary period, he is appointed as permanent employee of the organization.

Thus, all the above said steps of selection are important for the appointment of right kind of person for the right job.

19. Explain the merits and demerits of On-the-Job Training.

Answer.

Merits of On-the-Job Training

The merits of on-the-job training are stated below.

(i) It is an economical way of learning. Additional personnel are not required for training the employees when on-the-job method of training is used. Therefore, there is an advantage of economy by using this method.

(ii) The working centre itself serves as the learning centre. It is a great advantage in the sense that the trainee learns on actual working environment rather than on artificial environment.

(iii) It provides a favourable environment for quick learning since trainees are involved in the actual work process.

(iv) Employees feel at home in their surroundings.

(v) It is simple to learn the jobs that can be learned by watching and doing. Under it, the trainer need not explain and analyze the job detail, as employees can learn it by observing and doing it in the actual work station. It is learning by experience.

(vi) It is a flexible method.

Demerits of On-the-Job Training

The demerits of on-the-job training are stated below.

(i) The existing and experienced workers may feel troubled due to the interruption of both the trainees and the supervising members.

(ii) Trainer may not be experienced enough to train or he may not be so inclined. As a result, the quality of training may not be high.

(iii) Sometimes it becomes very difficult for the trainee to work as well as learn.

(iv) Sometimes, inexperienced handling of machines and tools by the trainees may result in colossal losses to the organisation.

(v) The productivity of employees who is undergoing training on-the-job may be dismal and disappointing in some cases.

20. What are the merits and demerits of Off-the-Job Training?

Answer.

The merits of off-the-job training are stated below.

(i) The trained employees are placed in the actual work station. As such, there remains the possibility of high productivity.

(ii) Here, the employees are trained outside the work environment. Consequently, they are not involved in production process. As a result, error in production can be minimized.

(iii) In off-the-job training, a large number of people can be trained at a time.

(iv) When the trainees are not involved in production process, the production activities can be carried out without any interruption.

(v) Costly errors and injuries can be avoided.

(vi) Trainers are usually experienced enough to train.

(vii) Sending an employee on a course could help to make an employee feel more valued.

The demerits of off -the-job training are stated below.

(i) This method of training may be very expensive due to extra space, accommodation and transportation costs and experts' fees etc.

(ii) It is not directly in the context of job.

(iii) Trainees may not be much motivated.

(iv) Employees may acquire new skills and leave the organization.

21. Define Control. Explain the steps in Control Process.

Answer.

Definition of 'Control'

Control is the process of evaluating and correcting activities to keep organization on course. According to Dale Henning, it is the process of bringing about conformity of performance with planned action. In the words of E.F.L. Brech, controlling is checking performance against predetermined standards contained in the plans with a view to ensuring adequate progress and satisfactory performance. According to Haynes and Massie, control is any process that guides activity toward some predetermined goal.

Process / Steps of Control

The process of control involves the following steps:

(i) Setting performance standards:

The first step in the control process is to establish standards against which results can be measured. Standards are used as the criteria or benchmarks by which performance is measured in the control process. Standards need to be flexible in order to adapt to changing conditions. The standards must be clear and easily understandable. Moreover, standards should be accurate, precise, acceptable and workable. It should not be either too high or too low. They should be realistic and attainable. Standards can be expressed both in quantitative and qualitative terms. Examples of quantitative standards include revenue to be earned, units to be produced and sold, cost to be incurred, time to be spent in performing a task etc. Examples of qualitative standards are improving motivation level of employees, improving labour relations, improving quality of products, improving goodwill etc.

(ii) Measurement of actual performance:

The second step in the control process is to measure the actual performance. Measurement of performance can be done by personal observation, by reports, charts and statements.

(iii) Comparing actual performance with standards:

After the measurement of the actual performance, the actual performance should be compared with the predetermined standards. If performance matches the standard, managers it can be assumed that "everything is under control".

(iv) Analysing deviations and taking corrective action:

This step becomes essential if performance falls short of standards and the analysis indicates that corrective action is required. After comparing the actual performance with the prescribed standards and finding the deviations, the next step that should be taken by the manager is to correct these deviations. Some deviations are possible in all the activities. However, the deviation in the important areas of business needs to be corrected more urgently as compared to deviation in insignificant areas. Management should use critical point control and management by exception in such areas. Corrective action should be taken without wasting of time so that the normal position can be restored quickly. The manager should also determine the correct cause for deviation. Control may reveal inappropriate standards and in such cases the appropriate corrective action could be a change in the original standards rather than a change in performance.

22. What are the prerequisites of an effective control system?

Answer.

The prerequisites of an effective control system are stated below.

(i) **Timeliness:** Many problems require immediate attention. If information about such problems does not reach the management in time, then such information may become of no use and damage may occur. Accordingly, control must ensure that information reaches the decision makers when they need it so that a meaningful response can follow.

(ii) **Flexibility:** The business and economic environment is highly dynamic in nature. Technological changes occur rapidly as well. As such, control system has to be flexible to adapt to the changing environment.

(iii) **Understandability and Acceptability:** Controls should be such that all people are able to understand them fully and accept them without hesitation. All members in the organisation should participate in the effective implementation of the control system.

(iv) **Emphasis on exception:** A good system of control should work on the exception principle so that only significant deviations are brought to the attention of management. This will eliminate unnecessary and uneconomic supervision and a waste of managerial time.

(v) **Fitting to the organizational culture –** The control system must fit the organizational culture. If the organization has a tight and bureaucratic system, a lose control will also not work.

(vi) **Economical–** Controls must be worth their costs. In simple words, cost of the control system should not exceed its benefits. Creating controls which are excessively expensive is counter-productive.

(vii) **Forward looking:** The system of control should be forward looking which enables the managers to keep a control on operations in advance.

(viii) **Regular revision:** The system of control must be revised regularly to meet the objectives of the organisation.

(ix) **Suggestive:** The control system should also be suggestive. A system which detects deviations only should not be held good, but should also tell the accurate and correct alternative.

(x) **Competent and talented staff:** Controlling A system of control can work more effectively if it has talented and competent people to work in the organisation.

(xi) **Objectivity:** The control should be objective, definite and determinable as far as practicable. The standards of measurement should be quantified as far as possible. If they are not quantifiable, such as training effectiveness etc. they must be determinable and verifiable.

(xii) **Motivating:** Control system should motivate both controller and controlled.

(xiii) **Corrective action:** An effective control system not only checks for and identifies deviation but also is programmed to suggest solutions to correct such a deviation in time.

23. Explain the principles of control.

Answer.

The main principles of control are listed below.

(i) **Principle of Reflection of Plans.** Controlling is the task of making sure that plans are carried out effectively. Therefore, control techniques must reflect the specific nature and structure of plans.

(ii) **Exception Principle:** The managers should concern themselves with exceptional cases i.e., those where the deviations from standards are very significant. Deviations of a minor mature may be left to subordinates for necessary action.

(iii) **Principle of Critical Points:** All operations have got' certain vulnerable or critical points. It is these which cause most of the troubles - give rise to major deviations. The managers should pay more attention to the guarding of these points.

(iv) **Principle of Prevention:** The truth of the saying 'Prevention is better than cure' is well-established. In control more attention should be directed to prevention of shortfalls than, remedying them after they occur. Feed forward control is very helpful in this respect.

(v) **Principle of Individuality:** Controls have to be consistent with the position, operational responsibility, competence, and needs of the individuals who have to interpret the control measures and exercise control.

(vi) **Principle of Flexibility:** If controls are to remain effective, flexibility is required in the design of controls.

(vii) **Principle of Standards:** Effective controls require objective, accurate and suitable standards.

Standards should earn the respect of people who have to abide by them.

(viii) **Principle of Reduced Controls:** A superior can spend less time in control activities if he has higher quality managers and their subordinates in his department.

(ix) **Principle of Efficiency:** Control techniques and approaches are efficient if they detect and illuminate the nature and causes of deviations from plans with a minimum of costs or other unsought consequences (Weihrich and Koontz).

(x) **Principle of Action:** Control is justified only if indicated or actual deviations from plans are corrected through appropriate planning, organizing, staffing, and leading (Weihrich and Koontz).

24. Define Communication. Explain the importance of Communication in an organization.

Answer.

Definition of 'Communication'

"Communication" is a **systematic process** of **exchanging** data, information, facts, ideas, opinions, feelings, emotions, news, views etc. through written or spoken words, symbols or actions between **two or more persons** for the purpose of bringing about **mutual understanding** with a view to **achieving organisational objectives**.

25. Explain the steps in Communication Process.

Answer.

The process of communication involves six steps:

(1) Idea formation

(2) Encoding

(3) Message transmission

(4) Message reception

(5) Decoding

(6) Feedback

The sender first develops / generates an idea. Encoding is the process of converting ideas into messages. After that, the message is transmitted by the sender to the receiver through appropriate communication channel. As soon as the message is received by the receiver, a relationship is established between the sender and the receiver. Then, the receiver decodes / deciphers the received message for understanding and interpreting the same. Finally, the receiver gives feedback.

26. Explain the different types of Organisational Communication.

Answer.

Different types of communication are explained below.

(a) According to organizational structure

(i) Formal Communication:

It is official in nature. It is rigid and static. It follows a prescribed path. It is reliable and dependable. It arises out of organizational needs. It is usually in written form.

(ii) Informal Communication

It is entirely unofficial. It is highly flexible and dynamic. It does not follow any prescribed path. Rather, it follows a zigzag path. It may not be as reliable as formal communication. It is very fast. It is mainly oral or gestural. It arises out of social and personal needs.

(b) According to expression

(i) Oral / Verbal Communication

Verbal / Oral communication refers to the form of communication in which message is transmitted verbally / orally. It is quick and prompt. Popular forms of oral communication include face-to-face talks, formal group discussions, and grapevine. It is more effective than written communication in conveying feelings, attitudes and reactions. This form of communication is more powerful because it not only includes speaker's words but also includes the changes in tone, pitch, speed and volume. It provides opportunities for immediate response. This mode of communication is useful when the information to be conveyed is short, the number of subordinate's small, the geographical distance between the sender and the receiver is short or the time available for communication is short. This is a natural form of communication during emergency situations.

(ii) Written Communication

Written communications are extensively used in organisations. The circulars, magazines, notes and manuals are some common forms of written communication. It is used for record and reference for future. It should be drafted clearly, simply, accurately and convincingly.

(iii) Gestural Communication

Gestural communication is all about the body language of speaker. It includes gesture**,** body language**,** posture**,** tone of voice or facial expressions etc.

(c) According to direction

(i) Vertical Communication

'Vertical communication' can be of two types: (1) Downward Communication, and (2) Upward Communication. Downward communication means the flow of communication from the top echelon (level or rank) of an organisation to the lower levels of employees. It helps in creating awareness among employees of the objectives, targets and goals. It also helps in establishing authority and discipline in the organization. But it may get delayed or distorted as it goes down through the various levels of the hierarchical set up. Upward communication is the flow of information from subordinates to superiors, or from employees to management. Employees can offer their suggestions, opinions, make complaints and seek redressal of their grievances through upward communication. It helps an organization to receive and reset its objectives at realistic levels. It flows from lower level of employees to higher-ups in the organisation.

(ii) Horizontal Communication

Communication among ***peer groups*** is called horizontal communication. It allows people with the ***same or similar rank*** in an organization to communicate with each other**.** ***Interdepartmental communication*** is an example of horizontal communication. For instance, communication between Sales Manager and Production Manager is an example of horizontal communication.

27. Distinguish between formal communication and informal communication.

Answer.

The differences between formal communication and informal communication are presented below.

SN	Points of Difference	FORMAL COMMUNICATION	INFORMAL COMMUNICATION
1	Flexibility	It is rigid and static.	It is highly flexible and dynamic.
2	Nature	It is official in nature.	It is entirely unofficial.
3	Flow	It follows a prescribed path.	It does not follow any prescribed path. Rather, it follows a zigzag path.
4	Reliability	It is reliable.	It may not be as reliable as formal communication.
5	Speed	It is slow.	It is very fast.
6	Type	It is usually in written form.	It is mainly oral or gestural.
7	Evidence	It has documentary evidence.	It is not backed by documentary evidence.
8	Secrecy	Secrecy can be maintained.	It is difficult to maintain secrecy.
9	Rumour	There is no scope for rumours.	It may contain rumours.
10	Cost	It is expensive.	It is less expensive than formal communication.
11	Distortion	Generally it is not distorted.	The possibility of distortion is very high.
12	Necessity	It arises out of organizational needs.	It arises out of social and personal needs.

28. Distinguish between verbal communication and written communication.

Answer.

The differences between verbal/oral communication and written communication are listed below.

Points of Difference	VERBAL/ORAL COMMUNICATION	WRITTEN COMMUNICATION
Meaning	Exchange of ideas, information and message through spoken words is Oral Communication.	Interchange of message, opinions and information in written or printed form is Written Communication.
Speed	It is fast.	It is slower than verbal communication.
Feedback	Immediate feedback is possible.	Feedback takes time.
Reliability	It is not as reliable as written communication.	It is more reliable.
Evidence	It is not backed by documentary evidence.	It is backed by documentary evidence.
Audience	It is suitable for small audience.	It is suitable for all types of audience.
Emergency	It is suitable for emergency.	It is not suitable for emergency.

29. What are the different types of barriers to communication?

Answer.

The different types of barriers to communication are listed below.

1) **Organisational Barriers:** Such barriers occur because of a) complex organisational structure, b) rigid organisational rules and regulations, c) unclear organisational policy, and d) information overload.

2) **Cultural Barriers**: These barriers arise due to cultural differences between the sender and the receiver.

3) **Perceptual Barriers:** Such barriers arise from perceptions that prevent people from communicating effectively.

4) **Physiological Barriers:** These barriers may result from individuals' personal discomfort, caused by ill-health, poor eyesight, or hearing difficulties.

5) **Emotional Barriers and Psychological Barriers:** Such barriers occur because of worries, stress, anger, anxiety etc.

6) **Language / Semantic Barriers:** These barriers arise due to the terminology used, use of specialized jargon, technical terms and abbreviations, unfamiliar accents etc.

7) **Physical Barriers:** Such barriers arise from physical distractions like background noise, poor lighting, uncomfortable sitting, and unhygienic room.

8) **Interpersonal Barriers:** These barriers are of two types**: a) Barrier from Superior** like Fear of losing power of control, Lack of trust, Shortage of time for employee etc. and b) **Barrier from Subordinate** like Fear of penalty, Lack of cooperation and mutual understanding, Lack of trust and coordination etc.

30. How to overcome barriers to communication?

Answer.

The different types of barriers to communication can be overcome in the following manner.

a) **Use of simple language:** Use of simple and clear words should be emphasized. Use of ambiguous words and jargons should be avoided.

b) **Reduction and elimination of noise levels:** Noise in any form is the main communication barrier which must be overcome on priority basis. It is essential to identify the source of noise and then eliminate that source.

c) **Simple organisational structure:** The organisational structure should not be complex. It must be as simple as possible.

d) **Avoiding information overload:** The communicators should not overload themselves with the information.

e) **Proper media selection:** The sender should properly select the medium of communication.

f) **Build a climate of trust and confidence:** It is absolutely essential to build a climate of trust and confidence between the sender and the receiver.

g) **Giving constructive feedback:** Negative feedback should be avoided. The contents of the feedback might be negative, but it should be delivered constructively.

h) **Active listening:** The receiver should be an attentive listener.

31. Define Coordination. Explain the features of Coordination.

Answer.

Definition of 'Coordination'

Co-ordination is the unification, integration, synchronization of the efforts of group members so as to provide unity of action in the pursuit of common goals. It is a hidden force which binds all the other functions of management.

According to Mooney and Reiley, coordination is an orderly arrangement of group efforts to provide unity of action in the pursuit of common goals.

Features of Co-ordination

(i) Essence of management: Coordination is not a distinct function but the very essence of management. It is inherent in managerial job and embodied in all the functions of management. Managers coordinate human and non-human resources, internal and external organisational environment, while carrying out the managerial functions of planning, organising, staffing, directing and controlling.

(ii) Managerial responsibility: Coordination is not the task of only top level managers but managers working at different levels try to coordinate the activities of organisation. The top level try to coordinate the overall plans and policies of organisation, middle level try to coordinate departmental activities and lower level coordinate the activities of workers.

(iii) Group effort: The concept of coordination always applies to group efforts. Coordination involves an orderly pattern of group efforts. It is relevant for group efforts and not for individual efforts. There is no need for coordination when only single individual is working.

(iv) Unity of action: Coordination ensures unity of action amongst individual and departmental activities. It ensures that activities of each individual, group and department are headed towards the common goal.

(v) Continuous process: Coordination is an ongoing function. It is a continuous function although its degree may vary. The managers work continuously to achieve coordination and maintain coordination because without coordination companies cannot function efficiently.

(vi) Common goal: Coordination maintains balance amongst individual, departmental and organisational goals. All individuals, groups and departments should have a common purpose, that is, achievement of the organisational goals. Coordination harmonizes conflicting departmental goals towards a common goal, that is, goal of the organisation.

(vii) Pervasive function: Coordination is required at all the levels and in all the departments of an organization.

32. Explain the principles for achieving effective Coordination in an organization.

Answer.

Mary Parker Follett has mentioned the following as important principles of co-ordination:

(i) **Principle of Early Beginning:** According to this principle, coordination must start at an early stage in the management process. It must start during the planning stage.
Principle of Continuity: According to this principle, coordination must be a continuous process. It must not be a one-time activity. Co-ordination is not a separate function and employing of each managerial function involves coordination. So management should make constant efforts to achieve co-ordination. It should not be left to a mere chance.

(ii) **Principle of Direct Contact:** According to this principle, all managers must have a Direct Contact with their subordinates. This will result in good relations between the manager and their subordinates. This is because direct contact helps to avoid misunderstandings, misinterpretations and disputes between managers and subordinates.

(iii) **Principle of Reciprocity**: This principle states that all factors in a given situation are interdependent and interrelated. For instance, in a group every person influences all others and is in turn influenced by others. When people appreciate the reciprocity of relations, they avoid unilateral action and co-ordination becomes easier.

33. Define Direction. Explain the principles of direction.

Answer.

Definition of 'Direction'

'Direction' is a process in which the managers instruct, guide and oversee the performance of the workers to achieve predetermined goals. It initiates action and it is from here the actual work starts. Direction is said to be consisting of human factors. In simple words, it can be described as providing guidance to workers in doing work.

Ernest Dale observed that direction is telling people what to do and seeing that they do it to the best of their ability.

Directing is a top-down approach. It is a vertical process in which orders come from the top for the subordinates to follow. Directing is person-centric.

Principles of Directing / Direction

(i) **Harmony of Objectives:** Harmonizing the individual's objectives with the group objectives is an important principle of directing. Individuals have their own objectives. An organization also has its own objectives. The management should coordinate the individual objectives with Organization objectives. Direction should be such that individuals can integrate their objectives with Organization objectives.

(ii) **Unity of Command:** An employee should receive orders and instructions only from one superior. If not so, there would be indiscipline and confusion among the subordinates and disorder will ensue.

(iii) **Direct Supervision:** It is essential for the managers to have a direct and personal contact with their subordinates because direction involves motivating the subordinates towards work. Direct supervision makes the subordinates happy and boosts their morale. It also ensures quick feedback of necessary information.

(iv) **Appropriate Leadership Style:** No single style is suitable to all situations. The style varies with the situations. Therefore, a manager should exhibit appropriate leadership style i.e., the style that is suitable to a given situation.

(v) **Use of Informal Organization:** Managers should make use of informal groups so that the formal groups can be strengthened.

(vi) **Use of Motivation Techniques:** Motivation ensures higher job satisfaction. Managers should use both monetary and non-monetary motivation techniques in order to ensure that the productivity and the quality of the products can be increased.

(vii) **Follow Up:** Directing is a never ending process. It requires continuous feedback which is essential to make necessary modifications in the activities of the management.

(viii) **Maximum individual contribution:** Every member's contribution is necessary for the organization's development. Hence the management should adopt a technique of direction which enables maximum contribution by the members.

(ix) **Effective control:** The management should monitor the behavior and performance of subordinates to exercise effective control over them. Effective control ensures effective direction.

(x) **Comprehension:** The extent of understanding by subordinates is more important than what and how orders are communicating to them. This is very useful in the proper direction of subordinates.

SECTION – B : MANAGEMENT
Study Note – 10
Management - Concepts

Learning Objective:

Any organization dedicated to achieving or accomplishing specific goals needs to a set of* management concepts. *Process means the primary functions or activities that management performs to get things done. These functions are planning, organising, staffing, directing and controlling.

I. Multiple Choice Questions

1. _____ is the right to act and extract obedience from others.

(a) Power

(b) Authority

(c) Responsibility

(d) None of the above

2. The process of assigning work to others and giving them authority to do is

(a) Control

(b) Organising

(c) Power

(d) Delegation of Authority

3. Delegation takes place between

(a) Superior and Subordinate

(b) Superior and Superior at same levels

(c) Subordinates and peers

(d) All of the above

4. Delegation may be
   (a) Specific or general
   (b) Written or implied
   (c) Formal or Informal
   (d) All of the above

5. What activity enables the managers to distribute their work load to others?
   (a) Centralisation
   (b) Decentralisation
   (c) Delegation of authority
   (d) None of the above

6. Delegation helps to improve the job satisfaction, motivation and morale of _____
   (a) Subordinates
   (b) Superiors
   (c) Peers
   (d) None of the above

7. Duty, authority and accountability are three fundamental components of:
   (a) Delegation of authority
   (b) Power
   (c) Control
   (d) Co-ordination

8. Duties should be assigned according to ____ of subordinates.
   (a) Qualifications
   (b) Experience
   (c) Aptitude
   (d) All of the above

9. Authority should _____ with responsibility.
   (a) Commensurate
   (b) Parity
   (c) More than
   (d) None of the above

10. _____ cannot be delegated.
   (a) Authority
   (b) Power
   (c) Responsibility
   (d) Accountability

11. Concentration of authority at the top level of the organization is known as ____
    (a) Centralisation
    (b) Decentralisation
    (c) Delegation of Authority
    (d) Responsibility

12. _____ means dispersal of authority throughout the organization.
    (a) Centralisation
    (b) Delegation of Authority
    (c) Decentralisation
    (d) None of the above

13. _____ is the end result which is achieved when delegation is systematically repeated up to the lowest level.
    (a) Decentralisation
    (b) Delegation
    (c) Centralisation
    (d) None of the above

14. Decentralisation is completed only when the fullest possible delegation is made at ___ of organization.
    (a) Lower levels
    (b) Top level
    (c) Middle level
    (d) All levels

15. Decentralisation suffers from the following limitation.
    (a) Relief to top executive
    (b) Expensive
    (c) Quick decision
    (d) Executive development

16. Span of Management is also known as
    (a) Span of Control
    (b) Span of Supervision
    (c) Span of authority
    (d) All of the above

17. ---------- represents the numerical limit of subordinates to be supervised and controlled by a single supervisor.
    (a) Unity of Command
    (b) Unity of Objective
    (c) Span of Control
    (d) Scalar Chain

18. Span of Control is based on the theory of relationships propounded by ___
    (a) Graicunas
    (b) George Terry
    (c) Barnard
    (d) Simon

19. There will be more organizational levels which in turn may impede communication, if the span of control is
    (a) wide
    (b) narrow
    (c) Optimum
    (d) None of the above

20. The supervisory load may become too heavy if the Span of Control is
    (a) Wide
    (b) Narrow
    (c) Optimum
    (d) None of the above

21. The term 'Power' is often considered as synonymous to
    (a) Responsibility
    (b) Accountability
    (c) Authority
    (d) Control

22. The ability or capacity to influence the behaviour or attitudes of other individuals is known as___
    (a) Power
    (b) Authority
    (c) Accountability
    (d) Responsibility

23. ____ is derived from position.
    (a) Accountability
    (b) Power
    (c) Authority
    (d) None of the above

24. The ability to grant or withhold rewards is a key source of ____ power.
    (a) Reward power
    (b) Coercive power
    (c) Referent power
    (d) Legitimate power

25. The ability to punish others for not carrying out orders or for not meeting certain requirements is known as ___ power.
    (a) Reward power
    (b) Expert power
    (c) Referent power
    (d) Coercive power

26. Coercive power is the opposite of
    (a) Expert power
    (b) Reward power
    (c) Referent power
    (d) Legitimate power

27. A teacher has ____ power over students.
    (a) Reward Power
    (b) Referent power
    (c) Expert power
    (d) Coercive power

28. Which is based on the personality attributes or personal virtues of a person?
    (a) Expert power
    (b) Referent power
    (c) Reward power
    (d) Legitimate power

29. Which is derived from the formal position of a person in the organization?
    (a) Expert power
    (b) Referent power
    (c) Reward power
    (d) Legitimate power

30. ____ is absolute and cannot be delegated.
    (a) Authority
    (b) Accountability
    (c) Responsibility
    (d) None of the above

31. Responsibility may be defined in terms of
    (a) Functions
    (b) Targets
    (c) Goals
    (d) All of the above

32. Responsibility flows in ____
    (a) Downward direction
    (b) Upward direction
    (c) All directions
    (d) None of the above

33. Subordinate is always responsible to his ___
    (a) Peers
    (b) Foremen
    (c) Management
    (d) Superior

34. The techniques to define responsibilities so as to actively involve members of an organization in its co-ordination effort are
    (a) Responsibility charting
    (b) Role Negotiation
    (c) PERT and CPM
    (d) Both (a) and (b)

35. Assignment of duties is meaningless unless adequate authority is given to _____.
    (e) Subordinates
    (f) Peers
    (g) Superiors
    (h) All of the above

36. _____ is the primary force within the organization which tends to lead it towards achievement of goals.
    (a) Decentralisation
    (b) Management
    (c) Centralisation
    (d) Delegation of authority

37. _____ is a philosophy of management.
    (a) Delegation
    (b) Decentralisation
    (c) Centralisation
    (d) All of the above

38. _____ implies diffusion of authority throughout the organization.
    (a) Delegation
    (b) Centralisation
    (c) Decentralisation
    (d) None of the above

39. Delegation helps to improve the job satisfaction, motivation and morale of _____
- **(a) Subordinates**
- **(b) Superiors**
- **(c) Peers**
- **(d) None of the above**

40. Delegation takes place between
- **(a) Superior and subordinate**
- **(b) Peers**
- **(c) Subordinates and peers**
- **(d) All of the above**

41. Authority and _____ should be co-extensive.
- **(a) Power**
- **(b) Responsibility**
- **(c) Accountability**
- **(d) Command**

Answer.

1	b	26	b
2	d	27	c
3	a	28	b
4	d	29	d
5	c	30	c
6	a	31	d
7	a	32	b
8	d	33	d
9	a	34	d
10	c	35	a
11	a	36	b
12	c	37	b
13	a	38	c
14	d	39	a
15	b	40	a
16	d	41	b
17	c		
18	a		
19	b		
20	a		
21	c		
22	a		
23	c		
24	a		
25	d		

II. True/False: State whether the following statements are True/False:

1. **The ability to grant or withhold rewards is a key source of power.**
2. **The term power is often considered as synonymous to Responsibility.**
3. **The authority given to a position is legal and legitimate.**
4. **Authority means ability to do something.**
5. **Authority can be visible from organizational chart.**
6. **Referent power is derived from the formal position of a person in the organization.**
7. **Responsibility arises from a superior-subordinate relationship.**
8. **Responsibility is absolute and can be delegated.**
9. **Responsibility chart is an important technique that can supplement the use of Role Negotiation.**
10. **Accountability arises out of responsibility and the two go together.**
11. **Responsibility flows downward.**
12. **A superior is always responsible to his subordinate.**

Answer.

1	True
2	False
3	True
4	False
5	True
6	False
7	True
8	False
9	False
10	True
11	False
12	False

III. Match the following

1.

	Column I		Column II
1.	Authority	(A)	Ability to do something.
2.	Teacher	(B)	Example for Referent Power
3.	Mahatma Gandhi	(C)	Right to do something.
4.	Non Financial Rewards	(D)	Example for Expert Power
5.	Power	(E)	Recognition and Status

Answer.

	Column I		Column II
1.	Authority	(C)	Right to do something.
2.	Teacher	(D)	Example for Expert Power
3.	Mahatma Gandhi	(B)	Example for Referent Power
4.	Non Financial Rewards	(E)	Recognition and Status
5.	Power	(A)	Ability to do something.

2.

	Column I		**Column II**
1.	**Responsibility Charting**	**(A)**	**Flows upward**
2.	**Responsibility**	**(B)**	**Flows in all directions**
3.	**Authority**	**(C)**	**Technique to define Responsibility**
4.	**Power**	**(D)**	**Superior and Subordinate**
5.	**Delegation of Authority**	**(E)**	**Flows downward**

Answer.

	Column I		Column II
1.	Responsibility Charting	(C)	Technique to define Responsibility
2.	Responsibility	(A)	Flows upward
3.	Authority	(E)	Flows downward
4.	Power	(B)	Flows in all directions
5.	Delegation of Authority	(D)	Superior and Subordinate

1. Define Authority and explain the characteristics of authority.

Answer.

Definition of 'Authority'

Authority is the right to guide and direct the actions of others and to secure from them responses which are appropriate to the attainment of the goals of the organization. According to **Henri Fayol,** authority is the right to give orders and the power to exact (get) obedience. It is the power to give orders and make sure that these orders are obeyed. A manager gets his authority from his position or post.

Characteristics of 'Authority'

The main characteristics of authority are stated below.

(i) It is not unlimited. The extent and limits of authority of a position are defined in advance.

(ii) It depicts the relationship between two individuals – one superior and the other subordinate.

(iii) It is used to achieve organizational goals.

(iv) Authority is formal, legal and legitimate.

(v) The individual or a group of individuals who possess authority are responsible to some higher authority. Accountability is the most significant characteristic of authority.

2. What are the different sources of power?

Answer.

The different sources of power are listed below.

(i) Legitimate Power: This is derived from the formal position of a person in the organization. Formal legitimate power is called authority.

(ii) Coercive Power: This is derived from a person's ability to create fear in another individual. It is based on the subordinate's expectation that punishment will be received for not agreeing or complying with the superior's commands or beliefs. Coercion may be direct or indirect, physical or psychological.

(iii) Reward Power: Reward power is the opposite of coercive power. Rewards may be financial, social or psychological. Financial rewards include salaries, wages, fringe benefits, etc. On the other hand, support, praise, recognition, status, etc., are non-financial rewards.

(iv) Expert Power: This is the power of knowledge, skill and expertise in certain areas. Physicians, lawyers and university professors possess such power.

(v) Referent Power: This is based on the personality attributes or personal virtues of a person. Such a person has a charisma which attracts people towards him. For example, Mahatma Gandhi became powerful and had a huge following due to his charisma.

3. Explain the differences between 'Power' and 'Authority'.

Answer.

The differences between 'Power' and 'Authority' are presented below.

S.N.	Authority	Power
1	It is given to a position or post.	It resides in the person who uses it.
2	It is always official in nature. So it is legitimate.	It need not be official in nature. So it need not be legitimate.
3	The scope of authority is narrow.	Power is a much broader concept than authority.
4	It flows downwards in the organisation.	It can flow in any direction.

4. Define 'Responsibility' and explain the characteristics of Responsibility.

Answer.

Definition of 'Responsibility'

'Responsibility' refers to an obligation of an individual to perform the duty assigned to him. George Terry opined that responsibility is the obligation to carry out assigned activities to the best of his abilities. The essence of responsibility is then obligation. A person who has authority has a corresponding responsibility for the proper exercise of authority given to him. Authority flows from a superior to subordinate while responsibility flows from a subordinate to a superior.

Characteristics of 'Responsibility'

The main characteristics of responsibility are stated below.

(i) It can be assigned to human beings only.

(ii) It arises from a superior-subordinate relationship.

(iii) It may be defined in terms of functions or targets or goals. As far as possible responsibility should be expressed in terms of targets. This will enable the subordinates to know by what standards their performance will be evaluated.

(iv) It is derivative of authority. When a subordinate is delegated authority he becomes responsible to his superior for the performance of assigned task and for proper use of delegated authority. Therefore, responsibility should be commensurate with authority.

(v) It is absolute and cannot be delegated.

(vi) It always flows upward. A subordinate is always responsible to his superior.

(vii) Accountability arises out of responsibility and the two go together. The person who accepts responsibility is accountable for his performance.

(viii) It may be continuing obligation or it may be discharged by accomplishing single task.

5. What are the different techniques to define Responsibility in an organization?

Answer.

Management can use various techniques to define responsibilities so as to actively involve members of an organization in its coordination effort. Two such techniques are: (1) responsibility charting, and (2) role negotiation. Moreover, new organizational positions may be created and line and staff conflict resolved by enhancing the degree of coordination.

1. **Responsibility Charting:** A responsibility chart is a nice way of summarizing the relationship between tasks and actors (performers). The chart lists activities that are complicated or the decisions that must be made and the individuals who are responsible for each of them. On the vertical axis we show the tasks and on the horizontal axis we show the actors.

The following four roles are important:

(i) The individual is responsible for the activity (decision).

(ii) The individual must approve the activity or decision.

(iii) The individual must be consulted before completing the activity or making the decision.

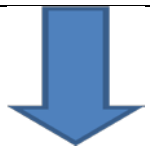
(iv) The individual has to be informed about the activity or the decision.

2. Role Negotiation: Role negotiation is an important technique that can supplement the use of responsibility charting. If used properly, it can lead to clear definitions of tasks and the responsibilities associated with them. The basic promise of the technique is that nobody gets anything without promising something in exchange. Organizational members meet at periodic intervals to list rededication of tasks so that coordination can be maximized. The primary objective of this approach is to identify the independent clusters of tasks completed by the organization. The second objective is to match the personal needs and work preference of individuals with the tasks that must be completed.

6. Briefly compare between Authority, Responsibility and Accountability.

Answer.

The comparison between authority, responsibility and accountability is summarised below in tabular form.

Points	Authority	Responsibility	Accountability
Meaning	It is the right to give orders and the power to exact (get) obedience.	It is the obligation to perform an assigned Task.	Being answerable for the final outcome is known as 'accountability'.
Origin/Source	It arises from formal Position.	The source is delegated authority.	It arises from responsibility.
Flow	 It flows downward.	It flows upward.	It flows upward.

7. Define Delegation of Authority. Explain the characteristics of Delegation of Authority.

Answer.

Definition of 'Delegation of Authority'

'Delegation' is an organizational process wherein the manager divides his work among the subordinates and gives them the responsibility to accomplish the respective tasks. Delegation does not mean avoiding decisions or abandonment of work. It does not mean abdication of responsibility. No manager can escape from his obligation by delegating authority to subordinates. Theo Haimann opined that delegation of authority merely means the granting of authority to subordinates to operate within prescribed limits.

Characteristics of Delegation of Authority

The important characteristics of delegation of authority are listed below.

(i) Delegation may be specific or general, written or implied, formal or informal.

(ii) Delegation does not mean avoiding decisions or abandonment of work.

(iii) Delegation does not mean abdication of responsibility. No manager can escape from his obligation delegating authority to subordinates.

(iv) A manager cannot delegate his/her total authority to the subordinates. He/she can delegate only a portion of it. Delegation does not mean that manager give up his authority, but he shares some authority with the subordinate essential to complete the responsibility entrusted to him.

(v) A manager cannot delegate the authority to a subordinate which he himself does not possess. It means that no one can give what he has not got.

(vi) Authority once delegated can be further expanded, or withdrawn by the superior depending on the situation.

(vii) A superior delegates his authority to a subordinate only for organizational purposes. He cannot delegate the authority to fulfil his personal objectives.

(viii) Delegation has dual characteristics. As a result of delegation, a subordinate employee receives authority from his superior, but, at the same time, his superior still retains all his original authority. George Terry comments on this concept: "It is something like imparting knowledge. You share with others who then possess the knowledge, but you still retain the knowledge too."

(ix) The extent of authority to be delegated depends upon several factors, like the ability and willingness of the executive to delegate, the ability of the subordinates to accept delegation, the confidence of the superior in his subordinates, the philosophy of management, etc.

8. Explain the importance of Delegation of Authority.

Answer.

The importance of delegation of authority is listed below.

(i) It facilitates quick decisions.

(ii) It helps in improving job satisfaction, motivation and morale of subordinates.

(iii) It reduces the workload of managers. With the process of delegation the managers can pass all their routine work to the subordinates and concentrate on important work. Without delegation managers will be overburdened with the work.

(iv) It facilitates organisational growth.

(v) It develops team spirit. Because of **delegation of authority**, efficient communication evolves amongst the superiors and subordinates. The subordinates are answerable to superiors and the superiors are responsible for the performance of employees. This improves relations and builds team spirit between the superiors and subordinates.

(vi) It acts as a training ground for management development. As a result of delegation employees get more opportunities to utilise their talents. It allows them to develop those skills which help them to perform complex task.

(vii) Delegation establishes the superior-subordinate relationship. Also, it directly relates to the extent and flow of authority. This is because authority determines who has to report to whom.

(viii) The superiors have confidence in subordinates and give them required authority. The subordinates accept their responsibility and this helps to develop cordial relationship between superiors and subordinates.

(ix) Delegation saves time allowing the employees to handle the challenges quickly. They can take the decisions speedily within their authority.

9. Explain the steps in the process of Delegation of Authority.

Answer.

The process of delegation involves the following steps:

1. **Determination of results expected:** First of all, a manager has to define the results he wants to obtain from his subordinates for achievement of organisational objectives.

2. **Assignment of duties:** Defining the work of the subordinates by their superior manager is known as assignment of duties. It also covers defining of the results expected from the subordinates. The manager may assign various duties in terms of goals, functions or results. As one manager cannot perform all the tasks, he must allocate a part of his work to the subordinates. Duties should be allocated according to the qualification, experience and aptitude of the subordinates.

3. **Granting of Authority:** If the delegated duties are to be discharged by the subordinates, they must be granted requisite authority for enabling them to perform such duties. Assignment of duties is meaningless unless adequate authority is given to the subordinates. Effective delegation, however, requires that the limits of authority should be made clear to each subordinate. The superior can delegate only that for which he has the authority and power to perform. He, however, does not give away the total authority; he only delegates a part of it, retaining the ultimate authority and responsibility to himself.

4. **Creation of Obligation or Accountability for Performance:** The last step in the process of delegation of authority is the creation of moral compulsion or obligation on the part of the subordinates for the satisfactory performance of their duties. The subordinates to whom authority is delegated must be made answerable for the proper performance of the assigned duties and for the exercise of delegated authority. The creation of obligation is, in real sense, an assumption of responsibility by the subordinates. By accepting an assignment (i.e. a delegated task), a subordinate, in effect, gives his promises to do his best in carrying out his duties. His obligation to do the task assigned makes him accountable to the delegator for discharge of his duties.

10. What are the difficulties in the Delegation of Authority?

Answer.

The difficulties in the delegation of authority may arise from the superiors or from the subordinates. These are explained below.

Difficulties from Superiors

(i) **Lack of Confidence in Subordinate: A** manager may not delegate authority because his feels that his subordinates are not capable and reliable. He lacks confidence in his subordinates.

(ii) **Fear of losing control:** When a manager is incompetent his work methods and procedures are likely to be faulty. He keeps all the authority to himself for fear of being exposed. He is afraid that if he lets the subordinates make decisions they may outshine him.

(iii) **Lure for authority: S**ome managers may not delegate authority because of their lure for authority. They are autocrats and think that delegation will lead to reduction of their influence in the organisation.

(iv) **Indispensable: S**ome managers feel that none can do the job as well as they can do. They consider themselves indispensable and do not want to give other people's ideas, a chance.

(v) **Lack of ability: A** manager is not likely to delegate authority when he cannot issue suitable directions to guide the activities of subordinates. Such lack of ability to direct shows that he is unfamiliar with the art of delegation.

Difficulties from Subordinates

(i) **Lack of self-confidence:** Subordinates may be reluctant to accept delegation when they lack self-confidence.

(ii) **Fear: A** subordinate who is afraid of committing mistakes and does not like to be criticised by the boss is likely to avoid delegation of authority.

(iii) **Additional responsibility:** When the subordinates are already overburdened with duties, they do not like additional responsibility through delegation.

(iv) **Lack of adequate information, working facilities and resources:** Subordinates are likely to avoid delegation when adequate information, working facilities and resources are not available for proper discharge of duties.

(v) **Absence of incentives:** Subordinates may not come forward to accept delegation of authority when no incentives are available to them.

11. Explain the differences between Delegation and Decentralisation.

Answer.

The differences between delegation and decentralisation are explained below.

(i) Delegation is a must for management as subordinates must be given sufficient authority to perform their duties. But decentralisation is optional in the sense that top management may or may not disperse authority.

(ii) Delegation is a technique of management used to get things done through others. However, decentralisation is a philosophy of management.

(iii) In delegation control rests entirely with the superior. But in decentralisation the top management exercises only overall control and delegates the authority for day today control to the departmental managers.

(iv) Decentralisation is much more than delegation. Delegation means transfer of authority from one individual to another. But decentralisation implies diffusion of authority throughout the organisation.

(v) Delegation is the cause of decentralisation. In other words, decentralisation is the result or effect of delegation.

(vi) In delegation the ultimate responsibility lies with the superior. But in decentralisation the ultimate responsibility lies with the departmental head.

(vii) In delegation the delegated authority can be withdrawn or taken back by the delegator at any time. But in decentralisation withdrawal of authority is not easy.

12. What are the advantages and disadvantages of decentralization?

Answer.

Advantages of decentralization

(i) **Quick decisions:** Decentralisation facilitates prompt decision which helps in avoiding delay and red tapism.

(ii) **Effective communication:** Under decentralisation, the span of management is wider and there are fewer hierarchical levels of organisation. Therefore, communication system becomes more effective.

(iii) **Relief to top executives:** Decentralisation helps in reduction of the workload of top executives. They can devote greater time and attention to important policy matters.

(iv) **Executive development:** When authority is decentralised, subordinates get the opportunity of exercising their own judgment. They learn how to decide and develop managerial skills.

(v) **Increased motivation and morale:** According to Louis A. Allen, "Decentralisation stimulates the formation of small cohesive groups. Since local managers are given a large degree of authority and local autonomy, they tend to weld their people into closely knit integrated groups." This improves the morale of employees as they get involved in decision-making process.

(vi) **Facilitates diversification:** Under decentralization, the diversification of products, activites and markets etc., is facilitated.

(vii) **Effective Control:** It is easier to measure the performance of the operations at the department level. This will lead to effective control.

(viii) **Better Co-ordination**: The various operations and activities are co-ordinated in a decentralised set up.

Disadvantages of decentralization

(i) **Expensive:** Decentralisation increases the administrative expenses. Each division or department has to be self-sufficient in terms of physical facilities and trained personnel.

(ii) **Lack of uniformity:** Decentralisation may lead to inconsistencies when uniform procedures are not followed by various departments.

(iii) **External constraints:** Decentralisation may not be possible due to external factors like market uncertainties, trade union movement, government intervention, etc.

(iv) **Difficulty in co-ordination:** Under decentralisation, each department or division enjoys substantial autonomy. Therefore, coordination among the departments becomes more difficult.

13. What factors should be taken into consideration while deciding the degree of decentralization in an organization?

Answer.

While deciding the degree of decentralisation in a particular organisation, the following factors should be taken into consideration:

(i) **Size and complexity of the organisation:** In a large and complex organisation there is greater need for decentralisation.

(ii) **Degree of diversification:** In a company having several diverse product lines, decentralisation is not only necessary but beneficial. High degree of standardisation, on the other hand, results in centralisation.

(iii) **Nature of functions:** Generally, basic functions like production and sales are more decentralized than staff functions such as personnel, finance, research and development.

(iv) **Dispersal of operations:** When the production and sales of an enterprise are geographically scattered, centralised control becomes very difficult and there is greater pressure for decentralisation of authority. But if all the activities are located in one building centralised control is much easier.

(v) **Availability of competent personnel:** It is advisable to decentralize authority only when managers at lower levels are able and experienced.

(vi) **Outlook of top management:** When the top executives believe in individual freedom, there will be a high degree of decentralisation. But if top management is conservative and prefers centralized control it is likely to centralize authority.

14. Write about Span of Management.

Answer.

Span of Management: It is also known as span of control, span of supervision or span of authority. It denotes the number of people a manager directly manages. In a wider span of control, a manager has many subordinates who report to him. In a narrow span of control, a manger has fewer subordinates under him.

Graicunas developed a formula to determine the span of management. It is shown below in tabular form.

Kind of Relationship	Formula
1. Direct single relationships (one-to-one relationships)	**n**
2. Cross relationships	**n(n-1)**
3. Direct group relationships	**$n(2^n/2 - 1)$**
4. Total Number of relationships (1+2+3)	**$n(2^n/2 + n - 1)$**

Illustration: A superior Tom has two subordinates, Dick and Harry.

- n = number of persons supervised
- a = number of direct single relationships (superior to subordinate)
- b = number of cross relationships (subordinate to subordinate - in both directions)
- c = number of direct group relationships (superior to combinations of subordinates)
- f = total of direct and group relationships (a + b + c)
- n = 2 (Dick and Harry)
- a = 2 (Tom to Dick and Tom to Harry)
- b = 2 (Dick to Harry and Harry to Dick)
- c = 2 (Tom to Dick, with Harry present; and Tom to Harry, with Dick present)
- f = 6 (a + b + c)

SECTION – B : MANAGEMENT
Study Note – 11
Leadership and Motivation

Learning Objective:

In this Chapter, Leadership and Motivation are discussed. As a leader, one should keep an open perspective on human nature. Knowing different needs of subordinates will certainly make the decision-making process easier. Motivation is a goal-oriented characteristic that helps a person achieve his objectives. It pushes an individual to work hard at achieving his or her goals. An executive must have the right leadership traits to influence motivation.

I. Multiple Choice Questions

1. The art of influencing others to direct their will, abilities and efforts to the achievement of goals is
- **(a) Directing**
- **(b) Motivation**
- **(c) Leadership**
- **(d) Staffing**

2. There can be no Leadership without
- **(a) Managers**
- **(b) Subordinates**
- **(c) Followers**
- **(d) Superiors**

3. Leadership process is interplay of three elements:
- **(a) The Leader, the follower and the situation.**
- **(b) The Leader, the followers and the subordinates.**
- **(c) The Leader, the followers and the superiors.**
- **(d) None of the above**

4. Leadership is a part of _____
- **(a) Organisation**
- **(b) Management**
- **(c) Both (a) and (b)**
- **(d) None of the above**

5. Autocratic Leadership is also known as
   (a) Authoritarian Leadership
   (b) Democratic Leadership
   (c) Free-rein Leadership
   (d) None of the above

6. The leader who exercises complete control over the subordinates is
   (a) Authoritarian Leadership
   (b) Democratic Leadership
   (c) Free-rein Leadership
   (d) None of the above

7. Which leadership style permits quick decision making?
   (a) Democratic Style
   (b) Laissez – Fair Leadership
   (c) Authoritarian Leadership
   (d) None of the above

8. Which style leads to frustration, low morale and conflict among subordinates?
   (a) Democratic Leadership
   (b) Authoritarian Leadership
   (c) Laissez Fair Leadership
   (d) None of the above

9. Democratic Leadership is also known as
   (a) Authoritarian Leadership
   (b) Free-rein Leadership
   (c) Laissez Fair Leadership
   (d) Participative Leadership

10. Leadership Continuum was developed by
   (a) Prof. Bernard
   (b) Prof. Terry
   (c) Tannenbaum and Schmidt
   (d) Stephen Robbins

11. Free-rein Leadership is also known as
   (a) Laissez Faire Leadership
   (b) Participative Leadership
   (c) Authoritarian Leadership
   (d) None of the above

12. Who avoids power and relinquishes the leadership position?
    (a) Autocratic Leader
    (b) Democratic Leader
    (c) Free Rein Leader
    (d) All of the above

13. Under which Leadership subordinates do not get the guidance and support of the Leader?
    (a) Free-rein Leadership
    (b) Autocratic Leadership
    (c) Participative Leadership
    (d) None of the above

14. ---------- leadership Style may be appropriate when subordinates are uneducated, unskilled and submissive.
    (a) Participative Leadership
    (b) Autocratic Leadership
    (c) Free-rein Leadership
    (d) None of the above

15. System 1 managers are
    (a) Exploitative Autocratic
    (b) Benevolent Autocratic
    (c) Consultative Autocratic
    (d) Democratic

16. System 2 managers are
    (a) Exploitative Autocratic
    (b) Benevolent Autocratic
    (c) Consultative Autocratic
    (d) Democratic Autocratic

17. According to Likert, which system of management is ideal system?
    (a) System 1
    (b) System 2
    (c) System 3
    (d) System 4

18. Under which system managers set goals and issue orders after discussing them with the subordinates?
    (a) Exploitative Autocratic
    (b) Benevolent Autocratic
    (c) Consultative
    (d) Democratic

19. Carrot and Stick approach to motivation is adopted under which system?
    (a) Exploitative Autocratic
    (b) Benevolent Autocratic
    (c) Consultative
    (d) Democratic

20. The system that adopts a paternalistic approach towards the subordinates is
    (a) Exploitative Autocratic
    (b) Benevolent Autocratic
    (c) Consultative
    (d) Democratic

21. Who conducted an extensive survey of management style and patterns in large number of organizations?
    (a) Rensis Likert and his associates
    (b) George Terry
    (c) Prof. Bernard
    (d) F .W. Taylor

22. The term 'Motivation' has been derived from the word.
    (a) Motivate
    (b) Motivated
    (c) Motive
    (d) None of the above

23. ___ means urge to do something.
    (a) Power
    (b) Motive
    (c) Authority
    (d) None of the above

24. The process of inducing or inspiring people to take the desired course of action means
    (a) Motivation
    (b) Staffing
    (c) Induction
    (d) Training

25. The process of motivation begins with
    (a) Fulfilment of Need
    (b) Discovery of need
    (c) Awareness of need
    (d) Search for action.

26. ____ involves interaction between needs and incentives.
    (a) Motivation
    (b) Control
    (c) Co-ordination
    (d) None of the above

27. Motivation is a ____ concept.
    (a) Psychological
    (b) Mental
    (c) Behavioural
    (d) N one of the above

28. Which of the following is not a financial incentive?
    (a) Pay
    (b) Allowance
    (c) Recognition
    (d) Bonus

29. Which of the following are non-financial incentives?
    (a) Participation in decision making
    (b) Challenging job
    (c) Recognition
    (d) All of the above

30. High motivation provides
    (a) Optimum utilization of resources.
    (b) Better industrial relations
    (c) Reduction in Labour Turnover (d) All of the above

31. Who developed a theory of motivation on the basis of hypotheses relating to human behaviour?
    (a) McGregor's
    (b) J. Stacy Adam's
    (c) Victor Vroom's
    (d) Herzberg

32. The theory that implies use of 'Carrot and Stick' Approach is
    (a) Theory Y
    (b) Theory X
    (c) Maslow's Need Hierarchy Theory
    (d) Herzberg's Model

33. Abraham H. Maslow, an eminent American Psychologist, developed a General Theory of Motivation known as
    (a) Theory X and Theory Y
    (b) Need Hierarchy Theory

(c) Herzberg's Two Factory Theory
(d) J. Stacy Adam's Equity Theory

34. _____ needs are at the base of the Hierarchy according to Maslow.
(a) Safety needs
(b) Esteem needs
(c) Physiological needs
(d) Self-actualisation needs

35. Need Hierarchy Theory is also known as
(a) General Theory of Motivation
(b) Victor Vroom's Expectancy Theory

(c) Theory X and Theory Y
(d) None of the above

36. Hierarchy of human needs –
(a) Physiological needs – Security needs – Social needs – Self Actualisation Needs – Esteem Needs
(b) Survival Needs – Safety Needs - Social needs – Esteem needs - Self Actualisation Needs
(c) Physiological needs – Social needs – Safety needs – Esteem needs - Self Actualisation Needs
(d) None of the above

37. Physiological needs are also known as
(a) Biological needs
(b) Survival needs
(c) Either (a) or (b)
(d) None of the above

38. Esteem Needs are classified into two types.
(a) Self esteem and esteem of others
(b) Safety and security needs
(c) Social needs and Esteem needs
(d) None of the above

39. The example of Physiological need is
(a) Pension Scheme
(b) Competence
(c) Work Groups
(d) None of the above

40. The example of Esteem Need is
(a) Reputation
(b) Recognition
(c) Achievement
(d) All of the above

41. Need for love and affection is ____
    (a) Survival needs
    (b) Social needs
    (c) Safety needs
    (d) All of the above

42. Maintenance factors are also known as
    (a) Hygiene Factors
    (b) Motivating Factors
    (c) Both (a) and (b)
    (d) None of the above

43. Identify the maintenance factors from the below:
    (a) Work itself
    (b) Recognition
    (c) Advancement
    (d) Salary

44. Identify the motivating factors from the below
    (a) Achievement
    (b) Opportunity for growth
    (c) Responsibility
    (d) All of the above

45. Maintenance Factors are called dissatisfiers.
    (a) True
    (b) False
    (c) Partly True
    (d) None of the above

46. Frederick Herzberg and his associates conducted interviews of ____ engineers and accountants in the Pittsburgh area of the United States.
    (a) 600
    (b) 200
    (c) 20
    (d) 2000

47. The distinction between maintenance factors and motivating factors is fixed.
    (a) True
    (b) False
    (c) Partly True
    (d) None of the above

48. Herzberg's Theory is an extension of ____
    (a) Theory X and Theory Y
    (b) Alderfer's ERG Theory
    (c) Victor Vroom's Expectancy Theory
    (d) Maslow's Need Hierarchy Theory

49. Maslow's Model is formulated in terms of
    (a) Human needs
    (b) Wants
    (c) Rewards
    (d) Goals

50. Herzberg suggested the use of ___ factors to avoid dissatisfaction.
    (a) Motivating factors
    (b) Environmental Factors
    (c) Maintenance Factors
    (d) None of the above

51. Work is natural like rest or play according to
    (a) Theory Y
    (b) Theory X
    (c) Theory X and Theory Y
    (d) None of the above

52. Blanchard and Hersey are associated with
    (a) Transactional leadership
    (b) Situational leadership
    (c) Transformational leadership
    (d) Leadership continuum

53. The ---------- theory/style of leadership suggests that no single leadership style is best.
    (a) situational
    (b) transactional
    (c) transformational
    (d) participative

54. The transformational leadership is --------- in nature.
    (a) proactive
    (b) reactive
    (c) situational
    (d) None of the above

55. A laissez-faire leader demands ----- feedback.
- **(a) more**
- **(b) less**
- **(c) immediate**
- **(d) None of the above**

56. One of the keys to situational leadership is----------.
- **(a) adaptability**
- **(b) rigidity**
- **(c) tenacity**
- **(d) All of the above**

57. The ---------- leadership style is suitable for turbulent environment.
- **(a) transactional**
- **(b) situational**
- **(c) transformational**
- **(d) All of the above**

Answer.

1	c	26	a	51	a
2	c	27	a	52	b
3	a	28	c	53	a
4	b	29	d	54	a
5	a	30	d	55	b
6	a	31	a	56	a
7	c	32	b	57	c
8	b	33	b		
9	d	34	c		
10	c	35	a		
11	a	36	b		
12	c	37	c		
13	a	38	a		
14	b	39	d		
15	a	40	d		
16	b	41	b		
17	d	42	a		
18	c	43	d		
19	b	44	d		
20	b	45	a		
21	a	46	b		
22	c	47	b		
23	b	48	d		
24	a	49	a		
25	c	50	c		

II. Fill in the blanks:

1. **The term 'motivation' has been derived from the word _____.**
2. **Motive means the urge to do _____.**
3. **Motivation is a _____ Concept.**
4. **Motivation is a _____ Process.**
5. **There is no -------- theory or approach to motivation.**
6. **_____ has developed a theory of motivation on the basis of hypotheses relating to human behaviour.**
7. **Theory _____ is based on a faulty conception of human nature.**
8. **_____ an eminent American Psychologist developed a General Theory of Motivation.**
9. **Esteem needs are of two types: self-esteem and esteem by _____.**
10. **Frederick Herzberg and his associates conducted interviews of _____ engineers and accountants in the Pittsburgh area of the United States.**
11. **Likert suggested that System ---------- is the ideal system towards which organizations should work.**
12. **Work is natural like rest or play according to Theory ---------.**
13. **System 2 managers are -------- autocratic.**
14. **The process of motivation begins with ------- of need.**
15. **Herzberg suggested the use of ------- factors to avoid dissatisfaction.**
16. **Leadership is a part of ----------.**
17. **---------- Leadership Style may be appropriate when subordinates are uneducated, unskilled and submissive.**
18. **High motivation provides optimum utilization of ----------.**
19. **Need for love and affection is ____ need.**
20. **Tannenbaum and Schmidt described ---------- points on the continuum to make it easy to understand how different leaders behave at different points on the continuum.**

Answer.

1. Motive
2. Something
3. Psychological
4. Continuous
5. universal
6. McGregor
7. X
8. Maslow
9. others
10. 200
11. 4
12. Y
13. benevolent
14. awareness
15. maintenance
16. management
17. autocratic

18. resources
19. social
20. seven

III. True or False:

1. **The art of influencing others to direct their will, abilities and efforts to the achievement of goals is called Leadership.**
2. **Autocratic Leadership is also known as Democratic Leadership.**
3. **The leader who exercises complete control over the subordinates is called Autocratic Leadership.**
4. **Leadership Continuum was developed by Tannenbaum and Schmidt**
5. **Participative Leadership Style may be appropriate when subordinates are uneducated, unskilled and submissive.**
6. **Carrot and Stick approach to motivation is adopted under Benevolent Autocratic system.**
7. **Maintenance factors are also known as Hygiene factors.**
8. **The distinction between maintenance factors and motivating factors is fixed.**
9. **Likert suggested that System 4 is the ideal system towards which organizations should work.**
10. **Work is natural like rest or play according to Theory X.**
11. **There can be no Leadership without subordinates.**
12. **The leader who exercises complete control over the subordinates is authoritarian leader.**
13. **Free-rein Leadership is also known as Laissez Faire Leadership.**
14. **System 2 managers are exploitative autocratic.**
15. **Power means urge to do something.**
16. **The process of motivation begins with fulfilment of need.**
17. **Safety needs are at the base of the Hierarchy according to Maslow.**
18. **Herzberg suggested the use of maintenance factors to avoid dissatisfaction.**
19. **Leadership is a part of management.**
20. **Motivation helps in combining the will to work with the capacity for work.**
21. **The situational theory of leadership suggests that no single <u>leadership style</u> is best.**
22. **The transactional leadership style views the leader-follower relationship as a transaction.**
23. **The transformational leadership is reactive in nature.**
24. **Blanchard and Hersey developed situational leadership theory.**
25. **In the Consultative Leadership Style, the manager has complete confidence and trust in subordinates and allows them a direct equal participation in decision making.**
26. **A laissez-faire leader demands more feedback.**
27. **The transformational leadership style is suitable for turbulent environment.**
28. **In situational leadership, the leader works for developing the existing organisational culture.**
29. **One of the keys to situational leadership is adaptability.**
30. **Motivation cannot be forced on employees.**

Answer.

1	True	11	False	21	True
2	False	12	True	22	True
3	True	13	True	23	False
4	True	14	False	24	True
5	False	15	False	25	False
6	True	16	False	26	False
7	True	17	False	27	True
8	False	18	True	28	False
9	True	19	True	29	True
10	False	20	True	30	True

IV. Match the following:

1.

	Column I		**Column II**
1.	**Motive**	**A**	**System 1 Managers**
2.	**Benevolent Autocratic**	**B**	**Urge to do something**
3.	**General Theory of Motivation**	**C**	**Abraham H. Maslow**
4.	**Free-rein**	**D**	**System 2 Managers**
5.	**Exploitative Autocratic**	**E**	**Laissez-Faire Leadership**

Answer.

	Column I		Column II
1.	Motive	B	Urge to do something
2.	Benevolent Autocratic	D	System 2 Managers
3.	General Theory of Motivation	C	Abraham H. Maslow
4.	Free-rein	E	Laissez-Faire Leadership
5.	Exploitative Autocratic	A	System 1 Managers

2.

	Column I		**Column II**
1.	**Theory X and Theory Y**	**A**	**Esteem Needs**
2.	**Self Confidence**	**B**	**Hygiene Factors**
3.	**Physiological needs**	**C**	**Social Need**
4.	**Need for Acceptance**	**D**	**McGregor**
5.	**Maintenance Factors**	**E**	**Survival Needs**

Answer.

	Column I		**Column II**
1.	Theory X and Theory Y	D	McGregor
2.	Self Confidence	A	Esteem Needs
3.	Physiological needs	E	Survival Needs
4.	Need for Acceptance	C	Social Need
5.	Maintenance Factors	B	Hygiene Factors

3.

	Column I		**Column II**
1.	Theory X and Theory Y	D	McGregor
2.	Self Confidence	A	Esteem Needs
3.	Physiological needs	E	Survival Needs
4.	Need for Acceptance	C	Social Need
5.	Maintenance Factors	B	Hygiene Factors

Answer.

	Column I		**Column II**
1.	Maslow	D	Need hierarchy theory
2.	Herzberg	A	Two-factor theory
3.	McGregor	E	Theory X and theory Y
4.	Likert	B	System 4
5.	Tannenbaum and Schmidt	C	Leadership continuum

4.

	Column I		**Column II**
1.	**Leadership**	**A**	**suitable when the subordinates are less competent**
2.	**Autocratic leadership**	**B**	**let them do**
3.	**Motivation**	**C**	**patriarchal, patronising system based on a master-servant relationship**
4.	**Laissez faire**	**D**	**Situation-specific**
5.	**Benevolent-Authoritative**	**E**	**is total, not piece-meal**

Answer.

	Column I		**Column II**
1.	Leadership	D	Situation-specific
2.	Autocratic leadership	A	suitable when the subordinates are less competent
3.	Motivation	E	is total, not piece-meal
4.	Laissez faire	B	let them do
5.	Benevolent-Authoritative	C	patriarchal, patronising system based on a master-servant relationship

5.

	Column I		Column II
1.	Leadership	D	Situation-specific
2.	Autocratic leadership	A	suitable when the subordinates are less competent
3.	Motivation	E	is total, not piece-meal
4.	Laissez faire	B	let them do
5.	Benevolent-Authoritative	C	patriarchal, patronising system based on a master-servant relationship

Answer.

	Column I		Column II
1.	Situational Leadership	B	Blanchard and Hersey
2.	Transformational Leadership	C	Proactive
3.	Transactional Leadership	D	Reactive
4.	Leadership continuum	A	Tannenbaum and Schmidt
5.	Exploitative--Authoritative	E	No confidence or trust in the followers

V. Answer following questions:

1. Define Leadership and explain the characteristics of Leadership.

Answer.

Definition of 'Leadership"

According to **Davis,** leadership is the ability to persuade others to seek defined objectives enthusiastically. It is the human factor which binds a group together and motivates it towards goals. **Koontz and O'Donnell** defined leadership as the ability of a manager to induce subordinates to work with confidence and zeal. In the words of **George R. Terry**, leadership is the activity of influencing people to strive willingly for group objectives. It is an important element of the directing function of management. According to **Warren Bennis,** leadership is the capacity to turn vision into reality.

Leadership is the art or process of influencing people so that they will strive willingly towards the realization of common goals. Leadership involves making sound (and sometimes difficult) decisions, creating and articulating a clear vision, establishing achievable goals and providing followers with the knowledge and tools necessary to achieve those goals.

Characteristics of Leadership

The main characteristics of leadership are listed below.

(i) Follower: The essence of leadership is followership. Leadership exists only with followers. There can be no leadership without followers.

(ii) A process of influence: Leadership tries to influence individuals to behave in a particular way. It is a process of influencing the behaviour, attitude and beliefs of the followers.

(iii) Accomplishment of organisational objectives: Leadership attempts to achieve the organisational objectives.

(iv) Personal quality: Leadership is a personal quality.

(v) Situation-specific: Leadership is related to a particular situation at a given point of time under a specific set of circumstances. Thus, leadership styles do change under different circumstances.

(vi) Inter-personal relationship: Leadership shows the interpersonal relationship between leader and followers.

2. Explain the qualities of a Successful Leader.

Answer.

The qualities of a successful leader are listed below.

(i) Creative thinking: The leader should be able to think in an innovative and creative way.

(ii) Communicating skill: He should have excellent communication skill. Leaders have to speak with and listen to the followers, respond to the questions and concerns and should be empathetic.

(iii) Good personality: The leader should possess good personality in order to earn respect from the followers.

(iv) Sense of purpose and responsibility: He should have a sense of purpose and responsibility so that the followers are encouraged.

(v) Emotional stability: The leader should have the capacity to control emotion.

(vi) Courage to accept responsibility: He should always be willing to accept responsibility without any hesitation.

(vii) Honesty and integrity of character: Effective leadership includes a strong character. Leaders exhibit honesty, integrity, trustworthiness and ethics.

(viii) Objective and flexible approach: his approach has to be objective and flexible. He must not be rigid in his approach. He should be prepared to accommodate other's viewpoints and alter his decision if need be.

(ix) Self-confidence and diligence: the leader should be self-confident and diligent.

(x) Commitment, passion and decisive mind: He must be committed. He should have passion. The leader must not be indecisive.

3. Explain the difference between Leadership and Management.

Answer.

The difference between 'Leadership' and 'Management' are explained below.

S.N.	Points of Difference	Leadership	Management
1	**Scope**	The scope of leadership is narrow. Leadership is a part of management.	The scope of management is wide and vast.
2	**Formality**	Leadership can be formal as well as informal.	Management is for formal and organized groups.
3	**Followers v Subordinates**	The leader has followers.	The manager has subordinates.
4	**Credit and blame**	The leader gives credit to the followers for success and takes the blame for failure.	The manager takes credit for success and puts blame on the subordinates for failure.
5	**Emphasis**	In leadership, the emphasis on inspiring the followers.	In management, the emphasis on managing activities.
6	**Change v stability**	Leadership brings change.	Management brings stability.
7	**Thinking**	Leaders think for the long haul.	Managers think short-term.
8	**Importance**	Leaders build relationships.	Managers build systems and processes.

4. Explain the different types of Leadership Styles.

Answer.

The different types of leadership styles are analysed below.

(i) Autocratic: This an extreme form of dominant leadership. Autocratic leaders make all the decisions and they make it alone. They don't need to consider anyone's opinions or ask for advice. They only command. This form of leadership is best in crisis situations, but it can be highly demoralizing for the followers.

Advantages

a) It facilitates quick decision-making.

b) It may bring positive result in case of an emergency.
c) It is suitable when subordinates are less competent.

Disadvantages

a) It leads to frustration and low morale among subordinates.
b) No development of subordinates takes place.
c) Potential and creativity of subordinates are not utilised.
d) Initiative level of subordinates goes down.

(ii) Democratic: Democratic leadership, also known as **participative leadership**, is a perfect blend of "autocratic" and "laissez-faire" leadership styles. This type of leader usually consults his followers before making a decision. It implies that followers can participate in the decision-making process. However, the authority to finalize the decision lies with the leader only. This is usually the "best" form of leadership since it offers the benefits of both extremes (laissez-faire and autocratic) while cancelling out the disadvantages of each.

Advantages

a) It improves the job satisfaction and morale of the employees.
b) Quality of decision improves.
c) It improves the decision-making ability of subordinates.
d) It helps in developing a positive attitude among the followers.
e) It reduces labour turnover and labour absenteeism.
f) It aids the leader to multiply his abilities through the contribution of his followers.

Disadvantages

a) It is time-consuming and may result in a delay in the decision.
b) The leader may pass the work to subordinates and abdicate responsibility.
c) Consultation with subordinates may be considered as sign of incompetence of leader.
d) It may not yield a positive result when subordinates prefer minimum interaction with the leader.

(iii) Laissez-Faire: Laissez-faire is a French word that translates to, "let them do." A laissez-faire leader "leaves" his followers to do as they will. The followers have to be highly experienced or trained individuals and they should not need dictations to do their job. A laissez-faire leader demands less feedback. This type of leadership can prove ineffective for those subordinates who need supervision to maintain productivity.

Advantages

a) It results in full utilisation of the potential and capacity of the employees.
b) It has a positive effect on the job satisfaction and morale of the subordinates.
c) Maximum scope for development of subordinates is there.

Disadvantages

a) It ignores the contribution of the leader.
b) Subordinates do not get the guidance and support of the leader.
c) Subordinates may work in a different direction and result in chaos.

5. Explain the Transformational and Transactional leadership styles.

Answer.

Transformational leadership style

Transformational leaders are committed to aid the organization in achieving its goals. That apart, they also help group members fulfil their potential. It can lead to higher performance and more improved group satisfaction than other leadership styles. At the same time, it can result in improved well-being among group members. This style was first described during the late 1970s and later expanded upon by researcher Bernard M. Bass. The main features of this leadership style are listed below.

(i) It is charismatic in nature.
(ii) It is proactive.
(iii) It is suitable for turbulent environment.
(iv) Here, the leader stimulates the followers by setting group interest as a priority.
(v) The focus is on innovation, team-building, motivation and collaboration with employees at different levels of an organization to accomplish change for the better.
(vi) Here, the leader works for transforming or changing the existing organisational culture.
(vii) The leader puts emphasis on needs, ideals, morals and values of the followers.

Transactional leadership style

Here, the leader-follower relationship is viewed as a transaction. In most situations, it involves the employer-employee relationship. And the transaction focuses on the follower completing required tasks in exchange for monetary compensation. One significant advantage of this leadership style is that it creates clearly defined roles. Employees clearly know what they are required to do and what they will be receiving in exchange for completing those assignments. It also allows leaders to offer a great deal of supervision and direction in times of need. However, one significant drawback of this leadership style is that it tends to stifle creativity and out-of-the-box thinking. In 1947, the style was first proposed by Max Weber. Later on, it was followed by Bernard Bass in the year 1981.

The main features of this leadership style are listed below.

(i) It is bureaucratic in nature.
(ii) It is reactive.
(iii) It works well in settled environment.
(iv) Here, the leader works for developing the existing organisational culture. This style is best described as "keeping the ship afloat."
(v) It creates clearly defined roles.

6. Explain the Situational leadership.

Answer.

The situational theory of leadership suggests that no single leadership style is best. Rather, it all depends on the situation at hand. It is flexible in the sense that it can adapt to the existing work environment and the needs of the organization. This leadership does not take into consideration the specific skills of the leader. Rather, the style of management is adjusted or modified to suit the needs of the organization. Adaptability is the key to situational leadership. Here, the leaders must be capable of shifting from one leadership style to another to meet the changing requirements of an organization and its employees. These leaders must possess the insight to realise when to modify their style of management and which leadership approach fits each new situation. In 1969, Blanchard and Hersey, in their classic book "Management of Organizational Behavior, developed situational leadership theory They suggested that there are four primary leadership styles:

(i) Telling (S1): Here, the leader tells people what to do and how to do it.
(ii) Selling (S2): Here, the leader "sells" his ideas and message to get group members to buy into the process.
(iii) Participating (S3): In this approach, less direction is offered by the leader and he encourages the group members to come up with new ideas and.
(iv) Delegating (S4): It is a hands-off approach. The leader has minimum involvement. Group-members make most of the decisions.

The theory identifies four different levels of maturity, including:

(i) M1: Group-members lack the knowledge, skills, and willingness to complete the task.
(ii) M2: Group-members are prepared and enthusiastic, but lack the capability.
(iii) M3: Group-members have the capability to complete the task, but are reluctant to take responsibility.
(iv) M4: Group-members are extremely skilled and eager to complete the task.

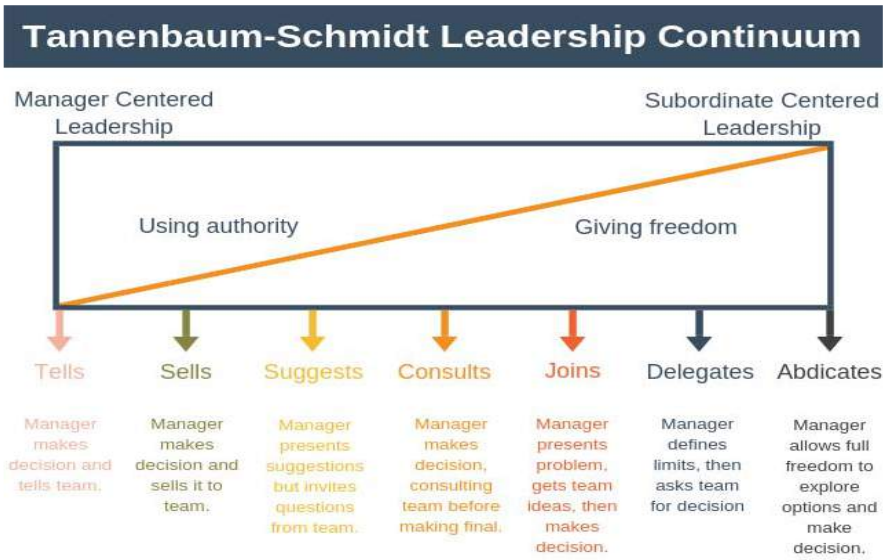
The model suggests that the following leadership styles are the most appropriate for these maturity levels:
(i) Low Maturity (M1)—Telling (S1)
(ii) Medium Maturity (M2)—Selling (S2)
(iii) Medium Maturity (M3)—Participating (S3)
(iv) High Maturity (M4)—Delegating (S4)

7. Write about Leadership Continuum.

Answer.

Robert Tannenbaum and Warren Schmidt wrote of the Leadership Continuum for the first time to highlight the range of possible leadership styles. According to them, the most effective leadership style is contingent on **three forces**, namely, **the leader, the follower and the situation**. At the left end of the continuum there is 'boss centred' (autocratic) leadership style while at the right end is the 'subordinate entered' (free-rein) - style. As one move from the left extreme to the right extreme, the degree of control goes down and the freedom of subordinates goes up. Most managers and leaders will lie somewhere in the middle between these two extremes.

The continuum of leadership behaviours is shown in the diagram below.



Source: https://expertprogrammanagement.com/2018/11/tannenbaum-schmidt-leadership-continuum/

Tannenbaum and Schmidt described seven points on the continuum to make it easy to understand how different leaders behave at different points on the continuum.

1. **Tells**
   The leader that tells is an authoritarian leader. He tells his team what to do and expects them to do it. This style is useful where deadlines are critical. However, this extreme style does not take into consideration the welfare of team members.

2. **Sells**
   The leader that sells makes his decision and then explains the logic behind the decision to their team. The leader is not looking for team input, but they are looking to ensure the team understands the rationale behind the decision.

3. **Suggests**
   The leader that suggests makes his decision, explains the logic behind the decision, and then asks team members if they have any questions. Through asking questions, the team can more fully understand the rationale behind the decision than the previous approaches. The leader is not going to change his decision but he wants the team to fully understand the rationale behind it.

4. **Consults**
   The leader that consults presents his provisional decision to their team and invites comments, suggestions, and opinions. This is the first point on the continuum where the team's opinion can influence or even change the decision. The leader is still in control and the ultimate decision maker, but the team also feels that they can influence the decision-making process.

5. **Joins**
   The leader who joins presents the problem to their team and then works with the team in a collaborative manner to make the decision. This point on the continuum differs from the previous four, as it is the first point the leader is not presenting his decision. Instead, he is simply presenting the problem to be solved. This obviously will require plenty of input from the team. As such, this style can lead to enhanced feelings of motivation and freedom.

6. **Delegates**
   The leader that delegates asks his team to make the decision, within limits that the leader sets. Although the team makes the decision, it is still the leader that is accountable for the outcome of the decision. It might seem very risky but the leader can limit the risk by specifying constraints. The leader should use this style only with very experienced teams.

7. **Abdicates**
   The leader who abdicates lets the team decide what problems to solve and how to solve them. Abdication is the total reverse of telling the team what to do using an autocratic style. This style can be the most motivating but can be disastrous if it goes wrong. Because of this, the leader should only use this approach with very experienced and senior people.

8. Explain about the Likert's System of Management.

Answer.

During the 1950s and 60s, Rensis Likert focussed his research interest in management. His 1961 book, '<u>New Patterns of Management</u>', proved highly significant. Likert identified four styles of management. The four systems are:

(i) System 1: Exploitative-Authoritative
Decision-making takes place at the top of the organization. These decisions are then imposed on others without consultation. There are very little teamwork and communication. Threats and fear are used for driving performance (motivation). Here, the leader or the manager has no confidence or trust in the followers or the subordinates. Subordinates do not have any freedom to discuss things about the job with their superior. In solving problems, the superior rarely gets ideas and opinions of subordinates. Here, communication is downward and interaction is virtually absent. Mediocre productivity was observed by Likert under this system.

(ii) System 2: Benevolent-Authoritative
This is a patriarchal, patronising system based on a master-servant relationship between the management and employees. Here, the leader or the manager has some confidence and trust in subordinates. Motivation is by way of with rewards and some punishments. Some upward communication is allowed. The superior solicits some ideas and opinions from subordinates. Further, some delegation of decision making is permitted but with close policy control. It is an improvement over System 1. Productivity is fair to good under this system.

(iii) System 3: Consultative

In this style, the manager has substantial but not complete confidence and trust in subordinates. However, he still intends to keep control of decisions. Subordinates can discuss things related to the job freely with their superior. The superior gets ideas and opinions from the subordinates and he attempts to use those ideas and opinions in a constructive manner. A reasonable amount of teamwork is there. There also exists some communication across and between levels. Productivity is good under this system.

(iv) System 4: Participative / Democratic

Here, the manager has full confidence and trust in subordinates. Subordinates are allowed to actively take part in the process of decision making. It leads to a collective sense of responsibility, collaborative teamwork and open communication. Productivity is excellent under this system.

Likert strongly believed that System 4 was the best system for managing an organisation. Likert observed style 3 and 4 as high producing while styling 1 and 2 as low producing. Likert also recommended extensive and intensive leadership training at all levels of management to reach style 4 as early as possible.

9. What are the measures to be taken for developing leadership ability of managers?

Answer.

The measures for developing leadership ability of managers are explained below.

(i) Leadership training: In order to expose managers to different leadership situations and teach them how to tackle those training programmes are undertaken. These situations are partially simulated and somewhat real. Through such training programmes, managers learn many things like (a) attitudes and behaviour they have to adopt in dealing with varied situations, (b) how to gain command over a situation, (c) how to inspire subordinates etc. It will help in injecting discipline and cohesiveness in the group. The managers under training are to be given immediate feedback on their leadership performance.

(ii) Internal organisational exposure: In order to develop the leadership aptitude of managers, they may be exposed to crucial situations within the organisation. Managers may be given the charge of particular committees responsible for the task of project implementation, coordination and control. Managers may also be placed in situations concerning people's problems. For example, the leadership quality of the managers may be tested by placing them in situations involving how to enhance the morale of a work group, how to resolve internal conflict etc.

(iii) Autonomy and accountability: Managers can sharpen their leadership capabilities under conditions of relative autonomy. They should be given ample independence to evolve their own methods of dealing with situations requiring critical leadership abilities. At the same time, they should be provided with the required organisational support in the form of authority, status, and top management support. They should be given adequate discretion within the framework of certain norms and rules.

(iv) Opportunities for interaction: Managers should be given opportunities to continuously interact with their subordinates. Availability to time is important in this regard. Many managers are extremely busy with their own work. As a result, they do not have enough time to talk or listen to their subordinates, to steer them, to realise their viewpoints and to build them up.

(v) Job Rotation: Job rotation will definitely sharpen the skills of the managers. They should be exposed to different job environments. It will enable them to develop their ability to cope up with those situations which do not require stereotyped approaches.

(vi) Setting Challenging but Realistic Goals: Goals set should be challenging. At the same time, those goals have to be realistic. There has to be a time-frame for the accomplishment of such goals. The goals should be set in such a way that they bring out and build up the best leadership abilities of managers.

10. What is meant by Motivation? Explain the characteristics of Motivation.

Answer.

Definition of 'Motivation'

According to **Dubrin**, motivation refers to expenditure of effort toward a goal. **Chung** defined motivation as goal directed behaviour. Goal directed behaviour is characterized by the process of selecting and directing certain actions among voluntary activities to achieve goals. According to **Hellriegel and Slocum**, motivation is a predisposition to act in a specific goal directed manner.

The term 'motivation' has been derived from the word 'motive'. Motive means the urge to do something. "Motivation' is a process of inducing or inspiring people to take the desired course of action. It is a process of stimulating people to actions to accomplish the goals. It is the driving force that inspires people to put their efforts willingly for the achievement of organisational goals. Motivation cannot be forced on employees. It comes automatically from inside the employees. It is the actuating force that stimulates a man to put his best in the accomplishment of a task. It is an integral part of the process of direction. Motivation involves interaction between needs and incentives. Incentives are the inducements which are used to motivate people. An incentive has motivational power because it helps to satisfy some need. Several financial and non-financial incentives are used to motivate people.

Characteristics of Motivation

The important characteristics of motivation are listed below.

(i) Motivation is total, not piece-meal: A person cannot be motivated in parts. An employee is an indivisible unit and his needs are interrelated. He cannot be motivated by fulfilling some of his needs partly.

(ii) Psychological concept: Motivation is a psychological phenomenon, which is generated within an individual in the form of an energetic force that drives him to behave or not to behave in certain ways. Motivation generates from within an individual. It starts and keeps individual at work

(iii) **Component of directing:** Motivating is an important component of directing functions of management. It is the responsibility of the managers to motive their subordinated to get all things done.

(iv) **Continuous process:** Motivation is an on-going process rather than one shot affair because an individual has unlimited wants and needs. These wants and needs cannot be satisfied at one time. As soon as the existing need is fulfilled, another will appear. Hence, motivation should go continuously.

(v) **Combining 'Will to work' with 'Capacity for work':** Motivation helps in combining the will to work with the capacity for work.

(vi) **Financial or non-financial:** The form of motivation depends upon the type of needs. Financial incentives include pay, allowances, bonus and perquisites. Non- financial incentives consist of recognition, praise, responsibility, participation in decision- making, challenging job, etc.

(vii) **Complex and dynamic process:** There is no universal theory or approach to motivation. Moreover, individuals differ in what motivates them. Motivation is a complex subject in the sense that the individual's needs and wants may be unpredictable. The level of need for a person depends on his/her psychological and physiological aspects.

(viii) **Goal-oriented:** Motivation is closely intertwined with behaviour. As a Behavioural concept, it directs human behaviour toward certain goals. A person behaves in such a way that he can satisfy his goals or needs. A person will work so long as he feels his actions are fulfilling his strongly felt needs. He will not pursue the activity and will lose interest in his work if he feels that it is not satisfying his needs.

(ix) **Positive or negative:** Positive motivation or the carrot approach offers positive incentives such as appreciation, promotion, status and incentives. Negative motivation or stick approach emphasizes penalties, fines and punishments.

(x) **Process:** Motivation is a process of inspiring, vitalizing and activating the employees to a higher level of performance. This process starts with unsatisfied needs. It moves through tension, drives and goal achievement. Finally, it ends with the reduction of tension aroused by unsatisfied needs.

11. Explain the importance of Motivation.

Answer.

Importance of Motivation

The importance of motivation is stated below.

(i) **Higher efficiency:** Motivation helps in enhancing the efficiency of the employees and of the organization. Motivated employees can perform with loyalty and enthusiasm.

(ii) **Better industrial relations:** Increased labour productivity results in higher wages for employees. Motivational schemes facilitate the integration of individual interests with organizational objectives. Motivation will foster team spirit among workers. This will reduce labour unrest and generate improved relations between management and workers.

(iii) **Decline in wastages and breakages:** Motivated employees take immense care in handling all resources of the organization. This will trim down wastages and breakages, thus resulting in higher benefits to the organization.

(iv) **Optimum utilisation of resources:** Motivation results in greater employee involvement and lesser wastages. This fosters optimum utilization of resources.

(v) **Drop in absenteeism and labour turnover:** The chance of remaining absent or leaving the organization is less when the employees are motivated. Motivation helps in developing a sense of belongingness amongst the employees towards the organization. As a result, overall performance improves.

(vi) **Helps in realizing organizational goals:** Motivation aids in the accomplishment of the objectives of the organization.

(vii) **Creation of a supportive work environment:** Motivation results in team spirit which helps in creating a supportive and congenial work environment.

(viii) **Improvement in the moral:** Motivation leads to improvement in the morale of the employees.

(ix) **Facilitating other functions of management:** Motivation acts as a facilitator of other managerial functions like planning, organising, staffing and controlling.

(x) **Helps in introducing changes:** High motivation helps to reduce resistance to change. An organisation has to incorporate changes to cope with environmental changes. Properly motivated employees accept, introduce and implement these changes keeping the organisation effective.

12. Briefly explain Maslow's Need Hierarchy Theory of Motivation.

Answer.

Features

The main features of Maslow's Need Hierarchy Theory of Motivation are stated below.

(i) Human needs are extensive in range, complex and interrelated.

(ii) Human needs form a particular hierarchy or priority structure in order of importance.

(iii) The lower-level needs have to be at least partially satisfied before one moves on to the higher-level needs.

(iv) As soon as one need is satisfied, the individual discovers another need which is still unfulfilled.

(v) A need that is satisfied ceases to be a motivator. Only unsatisfied need can motivate persons into action.

(vi) Every individual desire for moving up the need hierarchy. No one wishes to stop with the satisfaction of lower-level needs.

Different Types of Needs as per Maslow

Maslow identified five types of needs which are listed below.

(i) **Physiological needs:** These are biological needs required to preserve human life. Therefore, these needs are also known as survival needs. They include air, food, drink, shelter, clothing, warmth, sex, sleep etc. Physiological needs must be satisfied repeatedly but they are essentially finite. For example, an individual requires a limited amount of food but he requires it every day.

(ii) **Safety needs:** Safety needs are concerned with protection from danger, deprivation and threat. These needs are finite. Job security, financial security, protection from animals, family security, health security, etc. are safety or security needs of individual human being. Organisations can influence these needs through pension schemes, insurance plans etc.

(iii) **Social needs:** Man is a social animal as he seeks affiliation (association) with others. Social needs refer to the need for love, affection, care, belongingness, and friendship etc. Such needs are infinite as they are considered as secondary needs because they are not essential to preserve human life. They represent the needs of the mind and spirit rather than of the physical body. Organisations can influence these needs through supervision, communication system, workgroups, etc.

(iv) **Esteem needs:** Esteem needs are of two types: self-esteem and esteem of others. Self-esteem needs include self-respect, self-confidence, competence, achievement, knowledge and independence. Esteem of others includes reputation, status, and recognition. These needs are infinite and thwarting them results in feelings of inferiority, weaknesses and helplessness.

(v) **Self-actualization needs:** These are the needs for realising one's full potential, for continued self-development, for being creative. It is the desire of becoming what one is capable of becoming. It is an infinite and growth need. It is psychological in nature and very few persons satisfy it.

Criticism

The theory is widely criticised for the following reasons:

(i) The theory gives an over-simplification of human needs and motivation. Need recognition and fulfilment do not always follow the specific sequence of hierarchy suggested by Maslow. Need classification is somewhat artificial and arbitrary as human needs cannot be classified into neat watertight compartments. Therefore, the theory may not have universal validity.

(ii) The hierarchy of needs is not always fixed. Different people may have different orders. For example, in case of creative people like singers, painters, etc., self-actualisation need may become a dominant motivating force even before the lower order needs are satisfied.

(iii) There is no definite evidence that once a need is satisfied it loses its motivating force. It is also doubtful that satisfaction of one need automatically activates the next need in the hierarchy.

(iv) Needs other than those identified by Maslow also motivate people – for e.g. spiritual needs.

(v) The logic or sequence of the hierarchy differs from culture to culture.

(vi) Empirical research doesn't validate this theory.

(vii) Some persons will not aspire after their lower-order needs have been satisfied. Human behaviour is the outcome of several needs acting simultaneously. The same need may not lead to the same response in all individuals. Similarly, one particular behaviour may be the result of different needs. There is a lack of direct cause and effect relationship between need and behaviour.

13. Explain Herzberg's Two Factory of Motivation.

Answer.

Herzberg's Theory of Motivation tries to get to the root of motivation in the workplace. In the late fifties, Frederick Herzberg and his associates conducted interviews of 200 engineers and accountants in the Pittsburgh area of the United States. These persons were asked to relate elements of their jobs which made them happy or unhappy.

The two factors identified by Herzberg are motivators and hygiene factors.

1. **Motivating Factors:** The presence of motivators makes employees work harder. They are found within the actual work itself.

2. **Hygiene Factors:** The absence of hygiene factors will cause employees to work less hard. Hygiene factors are not there in the actual job itself but surround the job.

   Motivators are often referred to as factors for satisfaction, and hygiene factors are referred to as factors for dissatisfaction.

Motivating factors include:

(i) Achievement: A job must provide a sense of achievement to an employee. This will give a proud feeling of having done something hard but meaningful.

(ii) Recognition: A job must offer employee praise and recognition of their successes. Such recognition should come from both their superiors and their peers.

(iii) The work itself: The job itself must be exciting, diverse, and offer enough of a challenge to keep employees motivated.

(iv) Responsibility: Employees should "own" their work. They should hold themselves responsible for this completion and not feel as though they are being micromanaged.

(v) Advancement: Promotion opportunities should be there for the employee.

(vi) Growth: The job should offer employees the opportunity to learn fresh skills.

Hygiene factors include:

(i) Company policies: These should be fair and understandable to every employee.

(ii) Supervision: Supervision must be fair and proper.

(iii) Relationships: A healthy, friendly, and proper relationship should exist between peers, superiors, and subordinates.

(iv) Work conditions: Equipment and the working environment should be secure, fit for purpose, and hygienic.

(v) Salary: The pay structure should be fair, competitive and rational.

(vi) Status: The status of all employees within the organization should be maintained properly.

(vii)Security: Job security has to be ensured.

In a general sense, there are four states an organization or a team can find themselves in when it comes to Two-Factor Theory.

1. **High Hygiene and High Motivation:** This is the perfect situation and the one which every manager should attempt. Here, all employees are motivated and have very few complaints.
2. **High Hygiene and Low Motivation:** Here, the employees have not many grievances but they are not very much motivated. A situation where pay and working conditions are competitive but the work is not very exciting is an example of this.
3. **Low Hygiene and High Motivation:** Here, the employees are very much motivated but they have many grievances. A typical example of this situation is where the work is exciting but the pay and conditions lag behind that of the competitors in the same industry.
4. **Low Hygiene and Low Motivation:** This is obviously a terrible situation for an organization or a team to find itself in. Here, the employees are not stimulated and the maintenance factors are not up to scratch.

Criticism

(i) The difference between hygiene factors and motivating factors is not fixed. The same factor may be motivating for some people and maintenance factor for other people.

(ii) The theory puts more emphasis on satisfaction rather than on performance level. However, there is no direct link between satisfaction, motivation and performance. Therefore, Herzberg's two-factor theory is an oversimplified presentation of the process of motivation.

(iii) The theory is most applicable to knowledge workers. Studies of manual workers are less supportive of the theory. Therefore, the theory is not universally applicable.

(iv) The interview method used by Herzberg suffers from bias. The approach is highly subjective. Therefore, the empirical validity of the theory is doubtful.

14. Write about McGregor theory of Motivation.

Answer.

Theory X and Theory Y were first explained by social psychologist Douglas McGregor in his book titled "The Human Side of Enterprise".

Theory X

This style of management assumes that

- People are basically lazy and dislike their work. They will avoid work if possible.
- People want to avoid responsibility as much as possible and need constant direction.
- Workers have to be coerced, controlled, directed and threatened to deliver work.
- Workers need to be supervised at each step.
- People have no ambition.
- Workers lack creativity and resist change. They also lack self-motivation.

The above assumptions are negative in nature. Here, authority is seldom delegated, and control remains tightly centralized. The authoritarian leadership style is the most fitting leadership style in Theory X. This theory implies the use of a 'carrot and stick approach'.

Theory Y

This style of management assumes that

- Workers are happy to work on their own initiative.
- Workers are more involved in decision-making.
- People are self-motivated to complete their tasks.
- People seek and accept responsibility, and need a little direction.
- People view work as natural as play or rest.
- Workers solve problems in an innovative and creative way.

Theory Y advocates for democratic leadership style where the employees to have a greater say. Encouragement and rewards are used instead of control and coercion. Employees are provided with an opportunity to develop themselves. An organisation designed on the basis of Theory Y is characterised by decentralisation of authority, job enrichment, participative leadership and two-way communication system. The focus is on self-control and responsible jobs. Theory X places exclusive reliance on external control of human behaviour while Theory Y relies on self- control and self-regulation.

Criticism

Despite its significance, McGregor's theory has been criticised for various reasons. It tends to over-generalise and over-simplify people as being one way or the other. People cannot be put into two extreme patterns or stereotypes. The theory overlooks the complex nature of human beings. No human being belongs exclusively either to Theory X or to Theory Y. Theory X is perhaps visible in low paid or menial work but employees in those situations will move on in search of positions with Theory Y conditions if they are motivated. Personal development, management training and even general perceptions of behaviour are against a Theory X outlook towards work.

15. Distinguish between Theory X and Theory Y.

Answer.

The differences between Theory X and Theory Y are listed below.

Points of Difference	Theory X	Theory Y
Work	Workers dislike work	Work is as natural as play or rest to the workers.
Responsibility	Workers avoid responsibility.	Workers seek and accept responsibility.
Direction	Constant direction is required.	Little or no direction is required.
Control	Tight control is required.	Lenient control is required.
Ambition	Workers have little or no ambition.	Workers are highly ambitious.
Self-motivation	Self-motivation is absent.	Self-motivation is present.
Authority	Authority is centralised.	Authority is decentralised.
Leadership Style	Autocratic leadership style is used.	Democratic leadership style is used.
Creativity	Workers lack creativity and resist change.	Workers are creative and welcome change.
Focus	Focus is on lower level needs (Physiological and safety).	Focus is on both lower and higher level needs.

SECTION – B : MANAGEMENT
Study Note – 12
Decision Making

Learning Objective:

Decision making *is the process of* making *choices by identifying a* decision*, gathering information, and assessing alternative resolutions. Using a step-by-step* decision-making *process can help one to make more deliberate, thoughtful* decisions *by organizing relevant information and defining alternatives.*

I. Multiple Choice Questions

1. Who equated management with decision making because whatever a manager does is nothing but decision making?

(a) Felix M. Lopez

(b) John McDonald

(c) Andrew Szliagyl

(d) Herbert A. Simon

2. A decision to launch a new production plant is

(a) Programmed decision

(b) Non-routine decision

(c) Personal decision

(d) Organisational decisions

3. Which decisions are repetitive and routine in nature?

(a) Basic decisions

(b) Personal decisions

(c) Programmed decisions

(d) Non-programmed decisions

4. _____ decisions are concerned with unique problems or solutions.

(a) Basic decisions

(b) Organisational decisions

(c) Programmed decisions

(d) Personal decisions

5. A decision to attend a wedding ceremony is
   (a) Basic decision
   (b) Organisational decision
   (c) Programmed decision
   (d) Personal decision

6. Programmed decisions are made by
   (a) Lower level managers
   (b) Top level managers
   (c) Middle-level managers
   (d) None of the above

7. Non-programmed decisions are taken by
   (a) Lower-level managers
   (b) Top level managers
   (c) Middle-level managers
   (d) None of the above

8. Non-programmed decisions include
   (a) Decision to take over a sick unit
   (b) to restructure the existing organization
   (c) how to fill up the recently vacated position of zonal manager
   (d) All of the above

9. _____ decisions are those that are repetitive and routine.
   (a) Organisational decision
   (b) Non-routine decisions
   (c) Programmed decisions
   (d) Non programmed decisions

10. The first step in the decision-making process is:
   (a) Identification and diagnosing the real problem.
   (b) Evaluation of alternatives
   (c) Developing Alternatives
   (d) Selection of an alternative

11. The sequential set of steps in decision making is
   (a) Identification – Evaluation – Developing – Selection – Implementation.
   (b) Identification – Developing – Evaluation – Implementation – Selection.
   (c) Identification – Developing – Evaluation – Selection – Implementation
   (d) None of the above

12. The criteria for evaluating the alternative in decision making is:
    (a) Resources available for implementing the alternative.
    (b) Time constraint
    (c) Accomplishment of a common goal
    (d) All of the above

13. Who suggested, "Strategic factors refer to those that are most important in determining the action to be taken in solving a given problem".
    (a) Chester I Barnard
    (b) Louis Allen
    (c) George Terry
    (d) None of the above

14. What strategic factors should a manager has to consider while evaluating the alternatives?
    (a) Tangible
    (b) Intangible
    (c) Both (a) and (b)
    (d) Either (a) or (b)

15. Drucker mentions the following four criteria for selection of an alternative
    (a) Risk, economy of effort, timing and limitation of resources
    (b) Risk, economy of cost, timing and limitation of human resources
    (c) Value, economy of effort, timing and limitation of resources
    (d) Safety, value, timing and limitation of resources

16. The final step in the decision-making process is
    (a) Selection of an Alternative
    (b) Developing Alternative
    (c) Evaluation of Alternative
    (d) Implementation and follow up of decision

17. Decisions into programmed decisions and non-programmed decisions are adopted by
    (a) Peter Drucker
    (b) Herbert Simon
    (c) M. Lopez
    (d) John Mc Donald

18. _____ decisions refer to decisions techniques and rules.
    (a) Programmed decisions
    (b) Non-programmed decisions
    (c) Strategic decisions
    (d) Tactical decisions

19. The decisions which are made on situations and problems which are novel and non-repetitive are:
    (a) Programmed decisions
    (b) Non-programmed decisions
    (c) Strategic decisions
    (d) Tactical decisions

20. Strategic decisions are made at which level
    (a) Middle level
    (b) Lower level
    (c) Top level
    (d) At all levels

21. Strategic decisions include decisions on
    (a) Plant location
    (b) Introduction of new products
    (c) Acquisition of outside enterprises
    (d) All of the above

22. Tactical decisions are also known as
    (a) Operational decisions
    (b) Programmed decisions
    (c) Non-programmed decisions
    (d) Strategic decision

23. Tactical decisions are made to implement
    (a) Programmed decisions
    (b) N on-programmed decisions
    (c) Strategic decisions
    (d) Individual decisions

24. The disadvantage of group decision making are:
    (a) Delays in decision making
    (b) Lack of rationality and responsibility among group members
    (c) Dilution of the quality of decisions
    (d) All of the above

25. Which of the following are quantitative techniques of decision making?
    (a) Probability decision theory
    (b) Queuing theory
    (c) Simulation
    (d) All of the above

26. Which of the following are the modern techniques for non-programmed decisions?
    (a) Creative techniques
    (b) Participative techniques
    (c) Heuristic techniques
    (d) All of the above

27. Which is a sophisticated type of trial and error technique to find solutions to complex problems on a step by step basis?
    (a) Creative techniques
    (b) Participative techniques
    (c) Heuristic techniques
    (d) None of the above

28. PERT and CPM are _____ techniques.
    (a) Queuing Theory
    (b) Simulation
    (c) Linear Programming
    (d) Network

29. The technique for observing the behaviour of a system under several alternative conditions in an artificial setting is known as
    (a) Game theory
    (b) Simulation
    (c) Probability Decision Theory
    (d) Linear Programming

30. Brainstorming is one of the _____ techniques.
    (a) Creative
    (b) Participative
    (c) Heuristic
    (d) None of the above

31. The technique that involves the use of the brain to find different ideas which can solve a critical problem is
    (a) Participative technique
    (b) Heuristic technique
    (c) Creative technique
    (d) All of the above

32. The authority of taking organizational decisions may be delegated, whereas personal decisions cannot be ----------.
    (a) Decentralised
    (b) centralised
    (c) delegated
    (d) None of the above

33. Alex F. Osborn developed ---------- technique.
    (a) brainstorming
    (b) simulation
    (c) Delphi
    (d) queuing

34. Queues form because resources are -------.
    (a) plenty
    (b) limited
    (c) either a or b
    (d) both a and b

35. Policy decisions have ---------- impact on the functioning of the concern.
    (a) long-term
    (b) middle-term
    (c) short-term
    (d) very short-term

36. A bonus issue is a/an ---------- matter which is decided by the top management.
    (a) Operational
    (b) routine
    (c) personal
    (d) policy

37. In the case of group absenteeism ---------- decisions are required.
    (a) routine
    (b) non-programmed
    (c) programmed
    (d) operational

38. Olaf Helmer and Norman Dalkey were the first to develop the ---------- technique.
    (a) Delphi
    (b) Brainstorming
    (c) Heuristic
    (d) Simulation

39. ---------- is based on the premise that when people interact in a free atmosphere they will generate creative ideas.
    (a) Brainstorming
    (b) Probability
    (c) Delphi
    (d) Simulation

40. In the -------- technique, decisions are made on the basis of experience, common sense, rule of thumb etc.
    (a) Simulation
    (b) Brainstorming
    (c) Delphi
    (d) Heuristic

41. ---------- is the technique for optimization of an objective function under given resources and constraints.
    (a) Simulation
    (b) LP
    (c) Probability
    (d) Queuing

42. The decision maker should adopt a ---------- approach not only in making the decision but also after the decision has been put into implementation.
    (a) Rigid
    (b) flexible
    (c) static
    (d) either a or c

43. A possible alternative to brainstorming is ----------.
    (a) NGT
    (b) Simulation
    (c) LP
    (d) Probability

44. There are two powerful network techniques, namely, CPM and ----------.
    (a) LP
    (b) NGT
    (c) Simulation
    (d) PERT

45. ---------- is a technique for observing the behaviour of a system under several alternative conditions in an artificial setting.

(a) PERT
(b) Probability
(c) Simulation
(d) CPM

46. ---------- theory provides a basis for determining, under specified conditions, the particular strategy that will result in a maximum gain or minimum loss, no matter what opponents do or do not do.

(a) LP
(b) Game
(c) Queuing
(d) Probability

47. Which of the following is not an element of decision-making?

(a) Process
(b) Option
(c) Choice
(d) Model

48. Every ------- of a manager is generally an outcome of a decision.

(a) objective
(b) skill
(c) action
(d) power

Answer.

1	d	17	b	33	a
2	b	18	a	34	b
3	c	19	b	35	a
4	a	20	c	36	d
5	d	21	d	37	b
6	a	22	a	38	a
7	b	23	c	39	a
8	d	24	d	40	d
9	c	25	d	41	b
10	a	26	d	42	b
11	c	27	c	43	a
12	d	28	d	44	d
13	a	29	b	45	c
14	c	30	a	46	b
15	a	31	c	47	d
16	d	32	c	48	c

II. True or False:

1. **Brainstorming is one of the participative techniques.**
2. **Tactical decisions are made repetitively following certain established rules, procedures and policies.**
3. **Programmed decisions are of routine and repetitive nature which is to be dealt with according to specific procedure.**
4. **Policy decisions are of vital importance and are taken by the middle management.**
5. **The final step in decision making process is selection of an alternative.**
6. **Routine decisions are repetitive in nature.**
7. **Originally, the Delphi Technique was aimed at predicting the impact of technology on warfare.**
8. **Calculation of bonus is a policy decision which is taken at the lower levels to execute the policy decisions.**
9. **Decision pertaining to purchase of new factory premises is a major decision.**
10. **Critical factor analysis is helpful in developing alternatives.**
11. **The decision maker should adopt a flexible approach not only in making the decision but also after the decision has been put into implementation.**
12. **The Delphi technique is somewhat time-consuming, which renders it ineffective when fast answers are needed.**
13. **Queues form because resources are plenty.**
14. **In case of individual absenteeism programmed decisions can solve the problem whereas in case of group absenteeism non-programmed decisions are required.**
15. **Purchase of office stationery is a major decision which can be taken by office superintendent.**
16. **Acceptance of the decision by group-members will facilitate the smooth execution of decisions.**

Answer.

1	False
2	True
3	True
4	False
5	False
6	True
7	True
8	False
9	True
10	False
11	True
12	True

13	False
14	True
15	False
16	True

III. Fill in the blanks:

1. **_____ thinking is needed for solving novel, non-routine problems.**
2. **_____ is a technique for observing the behaviour of a system under several alternative conditions in an artificial setting.**
3. **The first step in decision making process is _____ and diagnosing the real problems.**
4. **Tactical decisions are also known as _____ decisions.**
5. **Strategic decisions are also known as _____ decisions.**
6. **Programmed decisions are of routine and _____ in nature.**
7. **_____ decisions are those which a manager takes in his official capacity.**
8. **Group decisions are also called as _____ decisions.**
9. **Matrices and Decision Trees are constructed to represent the _____.**
10. **The final step in decision making process is _____ implementation and ------- of the decision.**
11. **Every action of a manager is generally an ---------- of a decision.**
12. **A decision can be defined as a course of action consciously chosen from available --------- for the purpose of the desired result.**
13. **Programmed decisions are meant for routine and ---------- problems.**
14. **Policy decisions have ---------- impact on the functioning of the concern.**
15. **The authority of taking ------- decisions may be delegated, whereas personal decisions cannot be delegated.**
16. **According to Peter F. Drucker, ---------- factor analysis is helpful in identifying the causes of the problem properly.**
17. **Game theory is a technique of ---------- research.**
18. **The technique of ---------- was developed by Alex F. Osborn to help to bring creative ideas in the field of advertising.**
19. **Olaf Helmer and Norman Dalkey, scientists in RAND Corporation, were the first to develop the ---------- technique.**
20. **Queues form because resources are ----------.**

Answer.

1. Creative
2. simulation
3. identifying
4. routine
5. basic
6. repetitive
7. Organisational
8. collective
9. variables
10. follow-up
11. outcome
12. alternatives
13. repetitive
14. long-term
15. organizational
16. critical
17. operations
18. brainstorming
19. Delphi
20. Limited

IV. Answer following questions:

1. What do you mean by 'decision-making'?

Answer.

Every action of a manager is generally an outcome of a decision. Decision-making is a process involving information, choice of alternative actions, implementation, and evaluation that is directed to the achievement of certain stated goals. It may be defined as the selection of a course of action from among two or more possible alternatives in order to arrive at a solution for a given problem. According to George R Terry, decision-making is the selection based on some criteria from two or more possible alternatives. According to Peter F Drucker, "Whatever a Manager does, he does through Decision making..!" In the words of J.L. Massie, a decision can be defined as a course of action consciously chosen from available alternatives for the purpose of the desired result. Decision-making is a daily activity for any human being. When it comes to business organizations, decision-making is a habit and a process as well. Decision-making is a cognitive process that results in the selection of a course of action among several alternative scenarios. **Decision making is the process of making a choice between a number of options and committing to a future course of actions. From this definition, it is seen that there are four important elements of decision-making, namely,** process, options, choices and actions.

2. Explain the different types of Decisions.

Answer.

Routine and Strategic Decisions

Routine decisions are repetitive in nature. These decisions are related to the general functioning of the organisation. These decisions do not require any special effort. Generally, such decisions are taken by the middle and lower level manager. On the other hand, strategic decisions are taken by the top and middle-level managers. These decisions relate to policy matters. Such decisions are non-repetitive in nature. Usually, these decisions involve huge investments or funds.

Programmed and Non-programmed Decisions

Programmed decisions are meant for routine and repetitive problems. There exist specific or standard procedures for solving the problems. On the other hand, non-programmed decisions are meant for new, unstructured or badly defined problems or difficult situations. No standard procedures for handling such problems exist. These decisions require subjective judgements. Such decisions are made by top level management. For example, in case of individual absenteeism programmed decisions can solve the problem whereas in case of group absenteeism non-programmed decisions are required.

Policy and Operating Decisions

Decisions pertaining to various policy matters of the organisation are policy decisions. Policy decisions affect the entire enterprise. Such decisions are taken by the top management. These decisions have a long-term impact on the functioning of the concern. But operating decisions are taken by lower level management. These decisions relate to day-to-day functioning or operations of the business. For example, a bonus issue is a policy matter which is decided by the top management, but the calculations of bonus is an operating decision which is taken at the lower levels to execute the policy decisions.

Individual and Group Decisions

When a decision is taken by an individual in the organisation, it is known as an individual decision. Such decisions are generally taken in small organisations and in those organisations where the autocratic style of management prevails. Groups or collective decisions refer to the decisions which are taken by a group of organisational members, say Board of Directors or Committee. The main aim of taking group decisions is the involvement of a maximum number of individuals in the process of decision¬- making.

Organisational and Personal Decisions

When an individual takes a decision as an executive in the official capacity, it is known as an organisational decision. If the decision is taken by the executive in the personal capacity (thereby affecting his personal life), it is known as a personal decision. The authority of taking organizational decisions may be delegated, whereas personal decisions cannot be delegated.

Major and Minor Decisions

Another classification of decisions is major and minor. Decision pertaining to the purchase of new factory premises is a major decision. Major decisions are taken by top management. Purchase of office stationery is a minor decision which can be taken by the office superintendent.

3. Explain the Steps in decision making process.

Answer.

The steps in the process of decision-making are explained below.

(i) Identifying and diagnosing the real problems: The first step in the decision-making process is the identification of the problem. Diagnosing the problem implies knowing the gap between what we want to happen and what is likely to occur if no action is taken. As pointed out by Newman and Summer, identifying the cause of the gap' and understanding the problem solve the problem. According to Peter F. Drucker, critical factor analysis is helpful in identifying the causes of the problem properly. These factors are, in fact, obstacles in the way of finding a proper solution. These are also known as limiting factors. For example, if a machine stops working due to non-availability of the screw, the screw is the limiting factor in this case. A decision maker should collect as much information as possible before attempting to solve it. If possible, in addition to facts, the opinion should also be collected, which would aid in diagnosing the problem effectively.

(ii) Developing alternatives: After defining and analysing the problem, the next step is to develop alternative solutions. The main aim of developing alternative solutions is to have the best possible decision out of the available alternative courses of action. In developing alternative solutions the manager comes across creative or original solutions to the problems. In modern times, the techniques of operations research and computer applications are immensely helpful in the development of alternative courses of action.

(iii) Evaluation of alternatives: It the most important step in decision making. Here, the decision-maker draws the balance sheet of every alternative by identifying the advantages as well as disadvantages of these alternatives. All pertinent facts about each alternative should be collected, the pros and cons must be considered and the important points must be distinguished from the trivial or peripheral matters. Some of the criteria for evaluating an alternative could be —

(a) resources available for implementing the alternative
(b) economy of effort
(c) the element of risk involved
(d) results expected
(e) time constraint
(f) the accomplishment of a common goal
(g) implementation problems etc.

(iv) Selection of an alternative: The next important step in the decision-making process is the selection of the best alternative from various available alternatives. Indeed, the ability, to select the best course of action from several possible alternatives separates the successful managers from the less successful ones. Drucker mentions four criteria viz. the risk, the economy of effort timing, and limitation of resources before one alternative is selected among the available ones.

(v) **Implementation and follow-up of the decision:** The final step in the decision-making process is the implementation of the selected alternative in the organisation. The alternative selected should be properly communicated to those members of the organisation who are concerned with the decision. Decisions should be communicated in a clear, concise and understandable manner. Acceptance of the decision by group-members will facilitate the smooth execution of decisions. Further, after the implementation of the decision, it is necessary to follow-up to see whether the decision is yielding the desired results or not. Follow-up is indispensable so as to modify and improve upon the decisions at the earliest opportunity.

4. What are the quantitative techniques of Decision Making?

Answer.

Some important quantitative techniques of Decision Making are analysed below.

(i) **Linear Programming:** Linear programming is a quantitative technique used to determine the optimal mix of limited resources for maximizing profits or minimizing costs. It involves the solution of linear equations and is appropriate when the manager must allocate scarce resources to competing projects. It is the technique for optimization of an objective function under given resources and constraints. The objective function is either maximisation of some utility or minimization of some disutility. The technique is useful under conditions of certainty.

(ii) **Probability Decision Theory:** The basic premise of this theory is that the behaviour of the future is probabilistic and not deterministic. Various probabilities are assigned to the 'state of nature' on the basis of available information or subjective judgment and the likely outcomes of the alternative courses of action are evaluated accordingly before a particular alternative is selected. Pay-off Matrices and 'Decision Trees' are constructed to represent the variables.

(iii) **Game Theory:** Game theory is a technique of operations research. This provides a basis for determining, under specified conditions, the particular strategy that will result in a maximum gain or minimum loss, no matter what opponents do or do not do. Assume, a company has only one competitor and the size of the market is fixed; thus every gain in sales by one company means an equal loss in sales for the other. In an expanding market, both the companies could gain, in a declining market; one could gain at the expense of the other. Game theory has the greatest practical usefulness in planning sales promotion strategies.

(iv) **Queuing Theory:** Queuing theory deals with problems which involve queuing (or waiting). Typical examples might be:

- banks/supermarkets - waiting for service
- computers - waiting for response
- failure situations - waiting for a failure to occur e.g. in a piece of machinery
- public transport - waiting for a train or a bus

Queues are a common everyday experience. Queues form because resources are limited. Queuing theory helps in the design of balanced systems that serve customers quickly and efficiently but do not cost too much to be sustainable.

(v) Simulation: Simulation is a broad term indicating any type of activity that attempts to imitate an existing system or situation in a simplified manner. Simulation is basically a model building, in which the simulator is trying to gain understanding by replicating something and then manipulating it by adjusting the variables used to build the model. Simulation techniques are especially applicable to what-if problems, in which a manager or technician wants to know, If we do this, what will happen. Simulation can be conducted by the manipulation of physical models. For example, one might have a physical model of a machine and actually keep on increasing its speed to determine at what point it would begin to jam. It is a technique for observing the behaviour of a system under several alternative conditions in an artificial setting.

(vi) Network Techniques: There are two powerful network techniques—Critical Path Method (CPM) and Programme Evaluation and Review Technique (PERT) which are useful for project planning and control. Complex projects involve considerable cost and time. The objective is to minimise both by working out a 'critical path' where managerial attention is to be concentrated. A diagrammatic network of activities required for completion of a project is prepared in detail to assess their interrelation, to segregate sequential activities from simultaneous ones and to estimate the probable time and cost of their completion.

5. Explain the Modern Techniques for Non-Programmed Decisions.

Answer.

Some modern techniques for non-programmed decisions are listed below.

(i) Heuristic Techniques: Here, decisions are made on the basis of experience, common sense, rule of thumb etc. Heuristic techniques are developed by managers to deal with various components at different stages. Computers can easily be used in solving complex and strategic problems. In an uncertain environment and conflicting interests, the problem will have to be fragmented into small components for taking a realistic view. By splitting the problem into small parts and analyzing each part separately, a decision can be reached.

(ii) Participative Decision-Making:

It is a method of applying democratic means for the decision-making process. In participative decision-making, employees at various levels are involved in making various decisions. When subordinates are made a part of decision making, it not only helps in getting the advantage of their practical experience but also helps in implementing decisions properly. The subordinates feel motivated and encouraged and take an active interest in the working.

(iii) Brainstorming: It exposes a group of people to a problem and then allows them to generate ideas for a solution. All ideas are considered. The technique of brainstorming was developed by Alex F. Osborn to help to bring creative ideas in the field of advertising. Brainstorming is based on the premise that when people interact in a free atmosphere they will generate creative ideas. That is, as one person generates an idea, it serves to stimulate the thinking of others. This interchange of ideas creates an atmosphere of free discussion and spontaneous thinking. However, brainstorming sessions are time-consuming and, therefore, can be costly. Finally, brainstorming often produces superficial solutions.

(iv) Delphi Technique: The Delphi Technique started out as a technique to predict the future. It was developed by the RAND Corporation in 1950 for the US air force. Olaf Helmer and Norman Dalkey, scientists in RAND Corporation, were the first to develop the Delphi method. Originally, the Delphi Technique was aimed at predicting the impact of technology on warfare. For this decision-making method, a group of experts are asked to anonymously answer a survey and provide feedback on each other's answers. This process repeats itself. The aim is to come up with concrete solutions. The experts do not know each other and do not know who else is in the panel of experts. The technique is an iterative process, and first aims to get a broad range of opinions from the group of experts. The results of the first round of questions, when summarised, provide the basis for the second round of questions. Results from the second round of questions feed into the third and final round. It is a way of obtaining a collective view from individuals about issues where there is no or little definite evidence and where opinion is important. There are several advantages to the Delphi technique. One of the most significant is its versatility. The technique can be used in a wide range of environments, namely, government planning, business and industry predictions, volunteer group decisions. Another important advantage lies in the area of expenses. For example, the Delphi technique saves corporations money in travel expenses. The technique also protects participants' anonymity. Thus, they feel better protected from criticism over their proposed solutions and from the pitfalls of "groupthink", i.e., the withholding by group members of different views in order to appear in agreement. On the other hand, the technique has its drawbacks. The Delphi technique is somewhat time-consuming, which renders it ineffective when fast answers are needed. Further, results are dependent on the quality of the participants. The scientific nature of the method is sometimes questioned. The top experts may be difficult to recruit. Moreover, results can be influenced by the researcher.

(v) Nominal Group Technique

A possible alternative to brainstorming is 'Nominal Group Technique' **(**NGT). This technique was originally developed by Delbecq and VandeVen and has been applied to adult education programme planning by Vedros. This technique is a structured variation of small group discussion methods. The process prevents the domination of discussion by a single person, encourages the more passive group members to participate, and results in a set of prioritized solutions or recommendations.

6. Briefly explain the guidelines for effective decision making.

Answer.

One of the measures of effective management is the extent to which managers adopt effective decision-making processes to make decisions. A decision-making process and a decision are effective if it makes a significant contribution to the achievement of managerial and organisational objectives at acceptable levels of costs and unsought consequences. Within this broad setting, we may identify the principles, guidelines or the ways and means of making the process effective, as follows:

(i) Establishment of multiple decentralised centres: It is necessary to establish multiple decentralised centres of managerial decision-making at appropriate organisational levels.

(ii) Delegation of authority: It is essential to ensure delegation of adequate authority along with pinpointing of accountability for making decisions to managers at each centre.

(iii)

(iv) **Determination of work-load:** In order to minimise the possibility of overloading at any centre, determination of appropriate decision-making work-load at each centre has to be ensured.

(v) **Coordination:** Coordination of various decision-making centres through communication and other means has to be ensured so as to ensure consistency and co-operation in making decisions.

(vi) **Establishment of expert advisory staff units:** It is necessary to establish expert advisory staff units to provide the needed intellectual and professional inputs for decision making.

(vii) **Decision support systems:** Design and installation of decision support systems which include information and control systems are of utmost importance to provide logistic support to managers.

(viii) **Successful implementation of the decision:** Even the best decision will not yield satisfactory results unless it is implemented effectively. Successful implementation of a decision significantly depends on the extent of understanding of the decision and its implications, and motivation of the subordinates who have to carry it.

Flexibility: The decision maker should adopt a flexible approach not only in making the decision but also after the decision has been put into implementation. If it is not yielding the desired results, he should modify, discard, or replace it with another decision which may produce better results.

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