

# Business in the Market Economy

# 5

## Multiple Choice

- |        |         |         |
|--------|---------|---------|
| 1. (D) | 6. (B)  | 11. (A) |
| 2. (C) | 7. (B)  | 12. (C) |
| 3. (A) | 8. (C)  | 13. (D) |
| 4. (C) | 9. (A)  | 14. (A) |
| 5. (A) | 10. (C) | 15. (C) |

## Short Answers

### Question 1

- (a). Rapid Printing's productivity has declined from year 1 to year 2. In year 1, it was able to produce 140,000 units using 140,000 hours of combined employment across 10 machines (10 machines x 14,000 hours of employment per machine). This equates to 1 unit of production per hour in year 1. In year 2 however, Rapid Printing produced only 148,000 units using 220,000 hours of combined employment across 12 machines (12 x 18,500 hours). This equates to 0.67 units of production per hour in year 2 (148,000 units divided by 220,000 hours).
- (b). Production refers to the *total* amount of goods and services produced. Productivity refers to how much is produced with a *given quantity of resources*, per unit of time. In other words, productivity looks at quantities produced *relative* to the unit of input and time.
- (c). A firm may increase its productivity by adopting the latest technologies, especially information and communications technologies that can significantly reduce production times. Secondly, it may divide its labour into different parts of the production process, allowing the specialization of labour into sub-processes of production that will increase efficiency. An example of this is the assembly-line approach to car production. Finally, a firm may engage in large-scale production so that they can take advantage of highly specialized capital equipment and economies of scale in their production process.
- (d). Productivity improves economic growth and standards of living through greater efficiency in production that results in less wastage of scarce resources. Higher productivity will also lower inflation rates as firms can produce a greater quantity of goods and services at lower production costs. The economy would also experience an increase in its international competitiveness as increased productivity compared to foreign businesses will make Australia's goods more competitive, i.e. cheaper to sell on both local and international markets. Higher growth in a more productive economy will also support jobs and reduce unemployment.

### Question 2

- (a). What a firm produces may be influenced by the skills and experience of the business operator, who may wish to continue working in the same area. Second, it may be influenced by consumer demand for particular goods or services, as more demand creates more business opportunities.
- (b). A firm may maximise profits by reducing its costs of production, such as wages, rent and suppliers. Second, it can increase revenue through improving products and marketing.
- (c). Firms play a vital contribution to the performance of a market economy. The economic growth of an economy is ultimately tied to the growth of individual firms, as businesses are the source of production in an economy. Businesses that are growing will contribute to lower unemployment and higher wages. An increase in a firm's output will also increase the economy's productive capacity over time as firms are the main source of investment in an economy. This will allow an economy to achieve higher growth rates and improved living standards for its population in the future..
- (d). (d) Although profit maximisation is regarded as the main objective of businesses, a firm may have other goals it wishes to pursue which may either compliment or conflict with the profit maximisation objective. Public companies will have the goal of **meeting shareholder expectations** for maximizing the share price of a company that may at times conflict with profit maximisation. **Increasing market share** may be another objective of firms, particularly for larger businesses that may wish to expand their market position by acquiring other businesses. The cost and risk of expanding may conflict with a short-term profit-maximising objective. Another possible goal may be to **maximise the growth of a firm's assets**, which may occur at the expense of short-term profits. Finally, a firm may engage in **satisficing behaviour**, which it does not attempt to maximise any particular objective, but rather pursue satisfactory outcomes in all goals.

### Question 3

- (a). Should be marked in the middle of the curve at the point where the curve troughs.
- (b). The point should be between point A and the technical optimum, as specialisation of labour should cause per-unit production costs to decline.
- (c). Internal economies of scale refers to cost-saving advantages that result from the firm's own inside influences when the firm expands its scale of production. As a firm's operations increase in size, it is better able to take advantage of the specialisation of labour, invest in more efficient capital equipment, buy raw resources in bulk, and raise finance more easily for business expansion. External economies of scale on the other hand are cost-saving advantages that a firm enjoys as a result of *outside influences*, as opposed to the firm altering its own internal scale of operations.
- (d). (d) The first of the three production decisions a firm makes is what to produce, which will be determined by consumer demand, experiences of the business manager and other factors. The second question is how much to produce, which will be influenced by the level of consumer demand. The third question is how to go about producing using a combination of a range of factors of production that is most efficient for the firm's circumstances.
- (e). Technological change and investment can alter the productive capacity of a firm and often results in lower costs, increased efficiency and larger production runs. This assists in a firm's goal of maximizing profits, as well as meeting shareholder expectations to maximise shareholder returns, which are often tied closely to a firm's profits. However, substantial investment in technology is often very costly, and whilst this may lead to higher output growth and profits in the longer term, it may come at the expense of short-term profits. New technologies can also expand the range of products produced by a firm. An increase in innovation can result in a firm increasing its market share through producing a product that few competitors can match.

**Skills revision – pg.57**

*(in order of appearance from top to bottom)*

- internal economies of scale
- external diseconomies of scale
- external economies of scale
- external economies of scale
- external diseconomies of scale
- internal diseconomies of scale
- external economies of scale
- internal diseconomies of scale
- internal economies of scale
- internal diseconomies of scale
- internal economies of scale
- internal diseconomies of scale
- internal economies of scale
- internal diseconomies of scale
- internal economies of scale
- external diseconomies of scale