

Price Determination - E & M Value

Q.1. Write your opinion on the formation of cartels in an oligopolistic market structure.

Ans. Formation of cartels is a common practice in the oligopolistic market structure. It fosters economic interest of the members, as cartels facilitate monopolistic control of the market. Avoiding competition, the member firms are able to regulate supplies of the product in a manner that leads to higher price and abnormal profits. Lesser output at higher price implies sub-optimal use of the scarce resources and therefore, the loss of social welfare. It is owing to such negativities of cartels that even in the free market economies, the states often intervene to prevent their emergence. In India, Competition Commission is assigned the task of promoting competition and preventing the formation of cartels.

Q.2. Explain the economic value of support price policy in India.

Ans. The support price policy followed in India, particularly for food grains, assures the minimum income to the farmers and stable supplies of foodgrains in the market. It also helps the government to build buffer stocks of grains. The government can use these stocks when production is low on account of natural calamities (droughts and floods). However, the cost of storing wheat can be considered as the social cost of support price, along with the minimum price that the government pays to the farmers for the purchase of their produce. The government has to bear the financial burden of support price policy. At times, the financial burden may become so enormous that the government is forced to cut its development expenditure. A cut in development expenditure hampers the process of growth.

Q.3. Despite the fact that perfect competition offers maximum output at minimum price, it is not a perfect form of the market. Do you agree?

Ans. It is true that perfect competition is not a perfect form of the market. Because, under perfect competition, resources are allocated to different uses according to the criterion of profitability, NOT according to the criterion of social welfare. Those goods are produced of which prices are relatively higher and which offer higher profits. In this process, production of socially useful goods (as well as production of goods for the poorer sections of the society) is often neglected. Thus, while perfect competition leads to maximisation of output, it fails to achieve maximisation of social welfare.