C O R - Evaluation & Multi-Disciplinary

Q.1. In case of electricity which is sold by the government at a subsidised price, how can the government lower its losses without lowering the subsidy?

Ans. Losses are measured as the excess of cost over revenue related to a product. In a situation when subsidy is not reduced and, therefore, revenue cannot be raised through higher price of the product, the only way out to reduce losses is to lower the cost of production. The government must use more cost-efficient technology to produce electricity. Also, loss of revenue due to transmission losses and pilferage of electricity must be plugged.

Q.2. Small producers are often exempted from excise duty. Do you think this keeps their cost of production lower than the big producers and therefore, they earn higher profit per unit of output?

Ans. A cut in the excise duty reduces the average and marginal cost, leading to a rise in profit margin (other things remaining constant). However, this does not necessarily mean higher profit margin for the small producers compared to the big producers. Because, unlike small producers, big producers enjoy economies of scale leading to lower cost per unit of output. Often, the profit margins are found to be higher for the big producers than the small producers.

Q.3. How is the development of an SEZ (special economic zone) expected to influence the cost structure of a firm?

Ans. An SEZ offers multi-faceted infrastructural facility for the firms operating in the specified zone. It offers facilities of raw material, transportation, banking and insurance services. These facilities generate external economies for all the firms located in the SEZ. Because of the external economies, cost structure of an individual firm tends to be moderated. Unit cost of production is lowered.

Q.4. FDI not only brings investment in the domestic economy, it also brings new technology. How would the availability of new technology (relating to auto industry) impact the short period production function of a car manufacturer in India?

Ans. Short period production function of a firm is drawn on the assumption of a given technology. When new technology is available, the whole production function would shift: more output would be available from the same quantum of inputs. In terms of costs, firm’s AC curve would shift

downward. Thus, the availability of new technology (relating to auto industry) would shift the AC curve (of a car manufacturer) downward. It would prompt him to produce more at the going price.

Q.5. State one good, and one bad impact of ‘Make in India’ campaign on the cost structure of the domestic industry.

Ans. Good Impact

‘Make in India’ is expected to bring cost-efficient technology in the domestic economy. By using this technology, the domestic industry can hope to lower its cost structure.

Bad Impact

In response to ‘Make in India’ campaign, only big business companies are expected to come to the domestic market. These companies produce on a massive scale, and often emerge as the principal buyers of inputs in the domestic market. This may lead to a rise in input prices in the domestic market. Accordingly, the cost structure of the domestic producers may tend to rise.