9. How equilibrium price and output are determined by a firm under perfect competition?

The equilibrium is the point where economic forces are balanced and there are no external influences. The equilibrium is the condition where a market price is established through competition such that the amount of goods or services sought by buyers is equal to the amount of goods or services produced by sellers.

A perfectly competitive market has many distinguishing factors. A market in perfect competition has many people who are willing and able to buy a product as well as a many buyers who are willing and able to produce the products. The products the firms supply are exactly the same. Another distinguishing characteristic in a perfectly competitive market is that there are low entry and exit barriers to the market, and it is relatively

Under prefect competition how equilibrium price and output are determined this are given below ------

Large number of buyers and sellers: It is assumed that in pure competition market there should be a large number of buyers and sellers. If it is so, the output of any single firm is only a small proportion of the total output and each consumer buys small part of the total. Hence no individual purchaser can influence the market price by varying his own demand and no single firm is in the position to affect the market price by varying its own output.

Homogenous product: The commodity produced by all firms should be identical in pure competition. Thus the commodity produced by different firms are perfect substitutes. Hence the buyers are indifferent as to the firm from which they purchase.

Perfect competition is wider term than pure competition. Besides the two conditions of pure competition mentioned above several other conditions must be fulfilled to make it a perfect competition.

Free entry and exit: There should be no restrictions legal or other on the firms to entry and exit the industry. In this situation all the firms can earn only normal profit. Because if the profit is more than the normal, new firms will enter and extra profit will be reduced and if the profit is less than normal, some firms will leave the industry raising the profits for the remaining firms. Hence the firms can earn normal profit in long run.

Perfect knowledge: Another assumption of perfect competition is that the purchasers and sellers should have perfect knowledge about costs, price and quality. Due to this fact neither the seller can charge more than the ruling price nor the purchaser are willing to pay more.

Free mobility of the resources: The mobility of resources is essential to the firms in order to adjust their supply to demand. If the demand exceeds supply additional factors of production move into the industry and vice versa.

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10. Concepts of gross domestic product (GDP), Gross national product (GNP), and Net national product (NNP)

Definition of 'Gross Domestic Product - GDP'

The monetary value of all the finished goods and services produced within a country's borders in a specific time period, though GDP is usually calculated on an annual basis. It includes all of private and public consumption, government outlays, investments and exports less imports that occur within a defined territory.

GDP = C + G + I +
NX where:

"**C**" is equal to all private consumption, or consumer spending, in a nation's economy "**G**" is the sum of government spending
"**I**" is the sum of all the country's businesses spending on capital
"**NX**" is the nation's total net exports, calculated as total exports minus total imports. (NX = Exports - Imports)

GDP is commonly used as an indicator of the economic health of a country, as well as to gauge a country's standard of living. Critics of using GDP as an economic measure say the statistic does not take into account the underground economy - transactions that, for whatever reason, are not reported to the government. Others say that GDP is not intended to gauge material well-being, but serves as a measure of a nation's productivity, which is unrelated.

Definition of 'Gross National Product - GNP'

An economic statistic that includes GDP, plus any income earned by residents from overseas investments, minus income earned within the domestic economy by overseas residents.

GNP is a measure of a country's economic performance, or what its citizens produced (i.e. goods and services) and whether they produced these items within its borders.

Definition of 'Net National Product - NNP'

The monetary value of finished goods and services produced by a country's citizens, whether overseas or resident, in the time period being measured (i.e., the gross national product, or GNP) minus the amount of GNP required to purchase new goods to maintain existing stock (i.e., depreciation).

Alternatively, net national product (NNP) can be calculated as total payroll compensation + net indirect tax on current production + operating surpluses.

In other words, NNP is the amount of goods that can be consumed within a nation each year without reducing the amount that can be consumed in following years.

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11. Discuss the problems faced in estimating the GDP of a country?

First, GDP figures omit production of goods and services that are not sold on markets. This component includes housework, meals cooked at home, and child care provided by parents, as well as services volunteered for charities and other groups. For example, when parents care for their own children, the value of their care does not appear in GDP. However, when parents pay for child care, those services appear in GDP (for more examples see the book).

Second, GDP includes only a very imperfect estimate of production of goods and services sold on the underground economy (or black market). This activity includes production of illegal goods and services (such as drugs and prostitution). It also includes production of legal goods that goes unreported to avoid taxes. Many estimates suggest that the underground economy in the United States amounts to between 5 and 10 percent of GDP; this figure is even larger in many other countries.

Third, special measurement problems result when GDP includes certain goods that are not sold on markets. When you rent a house or apartment, your expenses appear in GDP as payments for housing services. However, if you own the house or apartment where you live, GDP includes the government's estimate of the rent that you would pay if you were renting.

Fourth: Substitution bias: As consumers' tastes change and as new technological improvements are introduced, the relative prices of goods change. Such changes are independent of inflation so optimally we would like the real GDP measure to take them into consideration. For example, as more people started using cellular phones, the cost of supplying this service went down and so has price. In the real GDP the value of these services is measured using old, higher prices, overstating the increase in the value of production.

New-good bias: it is very difficult to include new goods into the real GDP: In the base year they did not exist and hence their price was infinite.

Quality-change bias: if you simply take the number of TV sets produced and multiply it by the price of a typical TV set in the base year, the value of production is going to be underestimated, as this measure does not take into account the improvements in quality.

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12. What is meant by budget deficit?

A financial situation that occurs when an entity has more money going out than coming in. The term "budget deficit" is most commonly used to refer to government spending rather than business or individual spending. When it refers to federal government spending, a budget deficit is also known as the "national debt." The opposite of a budget deficit is a budget surplus, and when inflows are equal to outflows, the budget is said to be balanced.

Government budget deficits can be cured by cutting spending, raising taxes or a combination of the two. Deficits must be financed by borrowing money. Interest must be paid on borrowed funds, which worsens the deficit.

13. How can a deficit budget be financed? Give your answer in Bangladesh perspective?

A budget deficit occurs when government expenditure (G) is greater than revenue (T) (G>T).

There are several main ways that the Bangladesh government can finance a deficit.

i. Firstly, the government can borrow funds from the other sectors of the economy. This involves the selling of new Commonwealth Government Securities (CGS) such as treasury bonds through a tender system.

   This is the preferred government method of raising funds, as it does not add to net foreign debt, because the government is not borrowing from overseas. However, there is a disadvantage to this form of debt financing.

   When the Federal Government sells CGS it competes with the private sector for domestic savings, creating what is referred to as a "crowding out effect". A shortage of funds in the domestic market can result and domestic investors may need to borrow funds from overseas. Government borrowing has then, effectively "crowded out" private investment. Private investment may be postponed as interest rates and the cost of credit rise.

ii. The second possible method of financing a deficit is for the Commonwealth Government to sell CGS to the Reserve Bank. This form of borrowing from the Reserve Bank basically means that the government prints money to finance the deficit. The Government has not used this method of deficit financing since the deregulation of the Australian financial market in 1982. This is because it is highly inflationary: when the government spends the money, there is an increase in the money supply; if the economy is near full employment, demand inflation occurs rapidly, as there is too much money chasing a limited supply of goods.

iii. The third possible method used to finance a budget deficit is for the government to borrow funds from international financial markets. The government has not borrowed from overseas since the late 1980s to finance the deficit. When using this method, the Reserve Bank sells new CGS to overseas buyers, and receives foreign funds that are converted into Australian dollars. This method of financing the deficit adds to foreign debt when interest is paid on the securities (net income component of the balance of payments).

   The government may decide to borrow funds from overseas to reduce the crowding out effect. Under a floating exchange rate such borrowing has no effect on the domestic money supply. However, exchange rates and domestic interest rates can be affected; further, it adds directly to foreign debt.

iv. The selling of government assets is an alternative method to borrowing that the government can also use to fund a budget deficit. The sale of assets can create a headline budget surplus and reduce the crowding out effect typically caused by the sale of government bonds.

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14. Discuss the instruments of monetary policy?

The main monetary policy instrument of The bank is the key policy rate – interest rate applied in its main open market operations (currently, reverse repo transactions – repo sale of securities, with one-week transaction maturity). Other monetary policy instruments of The bank have a supporting role, facilitating unhindered transmission of the key policy rate effects to the market, as well as the development of the financial market. These instruments include:

open market operations,
required reserves,
lending and deposit facilities (standing facilities),
and Interventions in the foreign exchange market.

Monetary policy instruments do not have a direct impact on monetary policy objectives. As there can be a several months' lag in the effect of monetary policy, The bank focuses on the achievement of operating and intermediate targets. Operating targets are easy to control, but are remote from the ultimate objective, while intermediate targets are hard to control, but closer to the ultimate objective. As in the case of more developed market economies, and particularly those pursuing inflation targeting regime, the Banks operating target are interest rates in the interbank money market, and its intermediate target is the inflation projection.

Open Market Operations

The bank conducts open market operations in order to regulate banking sector liquidity, influence short-term interest rate movements and signal its monetary policy stance. The bank implements open market operations through repo or outright purchase and sale of securities.

Required Reserves

Required reserves are the amount of funds that banks are required to keep on deposit in accounts with the central bank.

Required reserves are calculated by applying the required reserve ratio to the reserving base. Required reserve base may be composed of all funding sources or a part of them It may be uniform or differentiated, according to maturity and/or currency structure of the funding sources.

Lending and Deposit Facilities (Standing Facilities)

Central bank's standing facilities include lending and deposit facilities available to banks on an ongoing basis. Overnight in maturity, these operations are initiated by commercial banks. Lending facilities include loans for maintaining daily liquidity, collateralized by eligible securities. Interest rates on standing facilities constitute the ceiling and floor of the corridor of interest rates in the interbank market. As an important control factor in managing banking sector liquidity, they ease the fluctuations of short-term interest rates in the interbank market which would be more pronounced without such facilities.

Interventions in the Foreign Exchange Market

In inflation targeting regime, foreign exchange interventions are an infrequently used secondary instrument which contributes to the achievement of the targeted inflation rate after the effective impact of the key policy rate has been exhausted.

Short Term Liquidity Loans Collateralized by Securities In addition to applying the above main monetary policy instruments, The bankalso approves to banks short-term liquidity loans against collateral of securities.

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