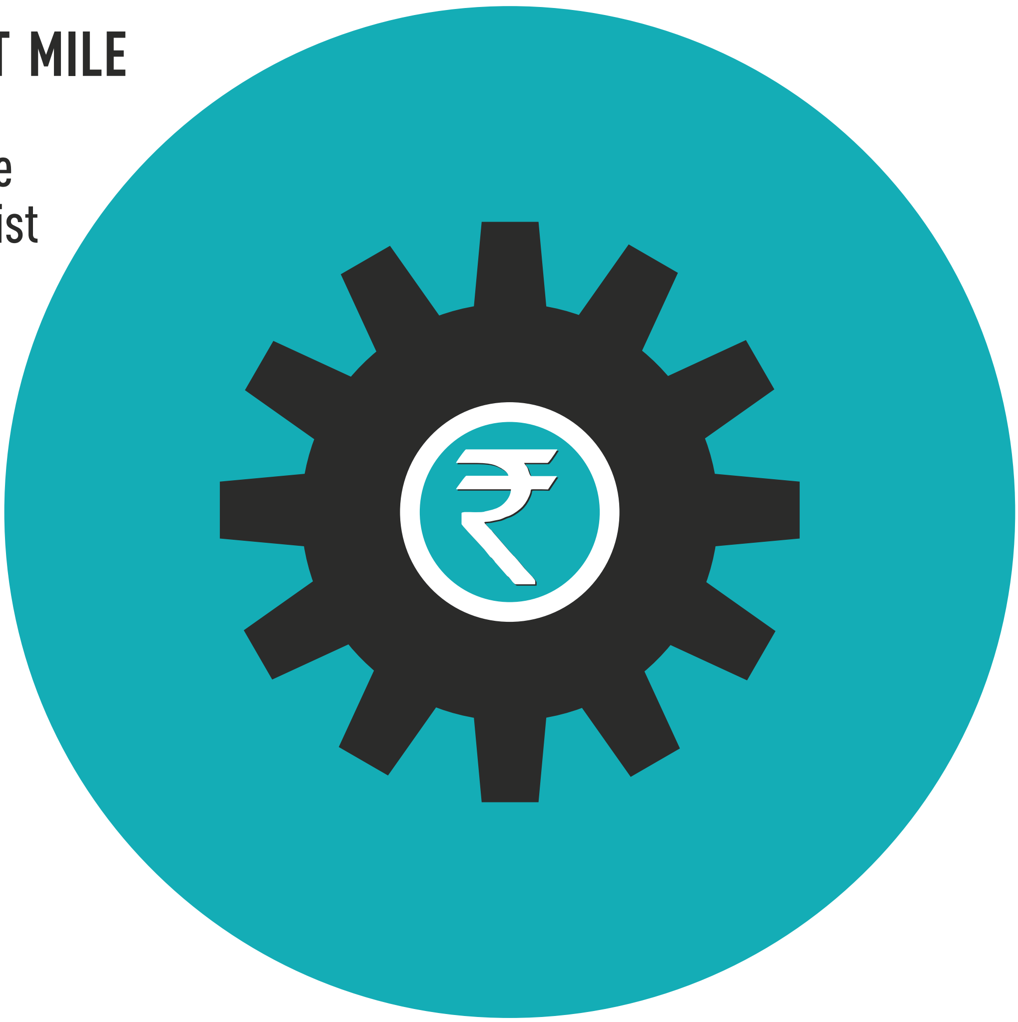
JUNE 2017 • Vol. 3 • Issue 3
MONTHLY • Pages 56
₹ 200

RNI No.: DELENG/2015/67140; Published on: Every month; Posted at Lodhi Road Sorting Office, New Delhi on every 1st week of the month

THE AWARE CONSUMER

www.consumerconexion.org

THE LAST MILE
Effects on Mixed, Free and Socialist Economies



OUT OF THE BOX
Contributing mechanisms in price discrimination

IN FOCUS
External factors determining prices of commodities

PRICE MECHANISM

Making the Right Choices and Reformation before the essence of trade and market is lost in an era of competition

PLUS ROUND UP • MY MARKET • THE PRESCRIPTION

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VIEWPOINT

BEJON KUMAR MISRA | bejonmisra@consumerconexion.org

PRICE MECHANISM

THE ECONOMISTS HAVE to deal with a large number of problems and it is their responsibility to decide the outcomes of every single step which is taken by the influential people in the market. They are the stakeholders and advisors who control the economic balance of a nation and make sure that an equilibrium is maintained under all circumstances. The world of trade and business comes across frequent imbalances and many businesses and firms are affected by these unexpected changes. One has to constantly monitor the change in policies and make necessary amendments in their own policies. One of the most threatening issues of the economy is limited amount of resources and unlimited wants of the society. It is rightly said that everything is available in sufficient quantity to fulfill the needs of the society, but it is insufficient to match the greed of the society. The more advancement is made in tools and techniques, the greater is the need of the society. We all are aware of the fact that all the needs cannot be fulfilled in the form of goods and commodities. It is also the responsibility of the society to understand that they are asking more as compared to the total amount of resources available in the country. As a responsible economist, one cannot ask each and every citizen of the country to compromise, because the resources will not stop getting depleted. But, so are the needs. There is a symbolic increase in the expectation of the people with rising standards of the services provided to them, and the market cannot take the risk of disappointing their consumers by cutting down the quality and quantity. There needs to be some system which keeps everything in an organized manner and always keeps back up in case of any emergency.

There is a symbolic increase in the expectation of the people with rising standards of the services provided to them, and the market cannot take the risk of disappointing their consumers by cutting down the quality and quantity.

The question arises about what to produce and in what quantities. Now, who will come forward and take the responsibility to answer these burning questions of the hour? By the time we try to sort out these basic questions, there is another group of voice that seeks an answer on how to produce. The ultimate aim here is to make you realize that economy is a huge term and it comprises of several factors. With each bygone decade, we come across an exceptional system to maintain the economy of a nation and the expectation keeps on increasing with passing time. The present condition of economy, on the global platform, demands the most efficient use of resources. When we look at a number of firms and industries, we realize that there is a geometric growth in their number over these many years. When we see the depletion of resources, we realize that they are being more exploited and less utilized for the production of finished goods. Again, the bottom-line is about making the choices and reformation as early as possible before the essence of trade and market is lost in the era of competition. The market solely works on the concept of demand and supply, and here is a revolutionary concept of price mechanism to do away with major problems of changes in economy.

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How Markets Work – The Price Mechanism

RESEARCH FEATURE

THE AWARE CONSUMER

UNLOCKING CONSUMER POTENTIAL
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JUNE 2017 • Vol. 3 • Issue 3

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The AWARE CONSUMER
is printed and published by
Bejon Kumar Misra
at F - 9, Second Floor, Kailash Colony,
New Delhi - 110048 and printed at
M/s. Spectrum Printing Press (P) Ltd.,
Shed No. 23, Computer Complex,
DSIDC Scheme I, Okhla Phase II,
New Delhi - 110020

Place of Publication: E - 45, Ground Floor,
Greater Kailash Enclave - I, New Delhi-110048

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Total number of pages - 56, Including Covers

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SR. PARTNER & MD, GLOBAL LEADER, MARKETING, SALES & PRICING PRACTICE, ATLANTA

Through comprehensive go-to-market transformation, companies we know are able to capture 10 percentage points or more of incremental growth. Some expand margins by 5 points or more.

ROUNDUP

IN THE ECONOMIC system of any country, there are a large number of resources which determines various key points of the economy. The most important factor in any kind of economy is capital, without which you cannot think or plan anything. The capital is a crucial factor because it keeps all the other elements active and functional. There are producers which are free to produce anything as per the demands of the population and on the other hand, there are consumers who are free to choose the product of their choice. Amidst all this, there is one factor which drives traffic towards a particular product and that is price.

In between the private producer and consumer, there is no interference from central authority to check capitalism. There is no certified authority to coordinate the inflow as well as outflow of capital between the producer and consumer. An absence of such authority can lead to an imbalance in the economy, which ultimately harms the entire system of any particular state or country. This is the point where price mechanism comes into play and substantiates the procedure. It lays down the process that lays down the points on what should be produced, how it should be produced and how much should be produced. When stepping into this domain of production business, it is important to keep in mind the risk factors and hurdles that will be imposed because of economic issues. Price mechanism keeps you aware of the things such as quality and quantity which are to be distributed amongst the consumers.

DATA BRIEFING

"India's gross domestic product is projected to expand 7.6% this year and next, the fastest pace among the world's major economies," the IMF said.

Price Mechanism

WITHOUT WASTING MUCH time, let us straight away see the definition of price mechanism. Price mechanism, in simple terms, is a system of deciding the price for goods and commodities based on the forces of demand and supply. The buyers and sellers are the major deciding factors that bring about a change in the pricing of goods and commodities. The market has the freedom to alter this pricing system by taking into account the demand and supply of particular goods. However, we have seen that government of a country can interfere and impose its own rules and regulations by setting up a central planning authority. These things are exclusively explained under the section of controlled price mechanism. The intervention of government is majorly to ensure that poor and deprived sections of the society are receiving the goods and commodities at an affordable price. For instance, government of India decides to decontrol the prices of diesel and the jurisdiction no longer has the role to play in it. In this situation, the prices will be solely determined by demand from consumers and supply from the oil companies.

The price mechanism is a part of market mechanism which has innumerable ways to balance the needs of both buyers and sellers. Here, the process is a sort of negotiation, where the pricing method can be adjusted as per the changing demands and supplies of goods and commodities in market. It is like announcing a bid and waiting for the genuine price to be fixed. The sellers or producers will tell the price they have decided for their product and buyers will express the prices they wish to pay for the same. The primary advantage of this method is that needs and expectations of both buyers and consumers are taken into account and then the price is fixed accordingly. After the things are finalized by the higher authority and conditions are laid out in advance, no third party can intervene in the transaction between buyer and seller. There is no further permission required from any other participant because if the buyer and seller are compatible with each other, the transaction occurs, in most cases automatically.

When we talk of price mechanism, it is important to note that increase in demand of particular goods will gradually increase its price in the market, thereby affecting the supply curve. We can consider the instance of oil crisis in 1970s to understand the concept behind pricing the products based on demand and supply. After the oil crisis, many nations started to produce their own oils due to dramatic increase in the price of oils. Since more nations were involved in their own oil production, the shortening in the supply of the oil soon recovered and the supply curve shifted to the right side. This indicated that there was more supply of oil and a balance was maintained again in the petroleum industry. The concept of price mechanism will be understood in a much better way if we understand the applications of pay and sell system in the market mechanism.

RATIONING

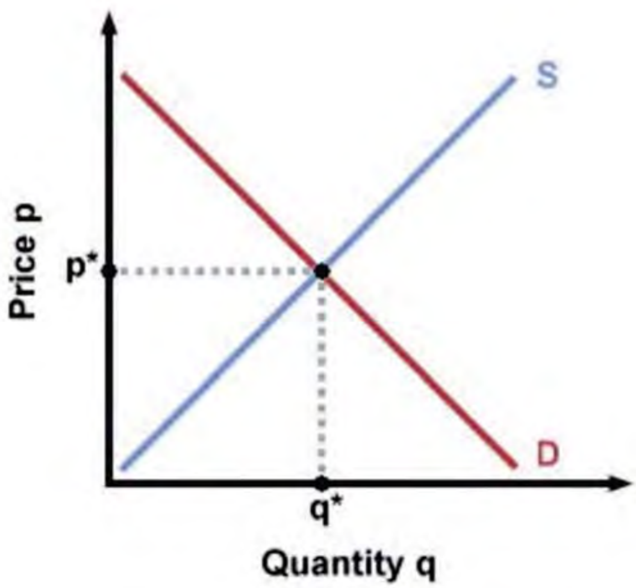
ONE CANNOT PREDICT much about the market and economy of a particular area. It is always necessary to have alternative arrangements to avoid loss in any kind of business. The consumers are the ultimate deciding factor about the fate and popularity of the goods or commodities which are being sold in the market. As per consumer psychology, it is unpredictable to decide whether one will have flourishing sale or a downfall in the market. This is because the buyers are always looking for the best and it is obvious that they will go where they see more crowds. In this context, it becomes important to be ready for anything and everything. You may fall short of the goods or you may see plenty of them remaining unsold. In either of the two cases you must have a plan to leverage the profit in your business. For example, if you are lacking resources but the demand is more than supply, you must think of ways to earn profit and slow down the pace of increasing demand. This may sound really weird and risky, but that is what business is all about. On the other hand, you may have plenty of goods and commodities but the demand will not be sufficient to fetch you enough profit. In this situation also, you must be prepared with a back-up plan to increase your sale without compromising with the quality of the product.

After looking at the possibilities, it seems quite feasible to manage plenty of goods but difficult to handle the lack of the same. Hence, there is one method through which one can overcome this period of goods shortage, and that is by switching over to a rationing function of price. This is a very important part of price mechanism because it helps you to keep your profit analysis intact despite having insufficient resources. Rationing function of price, in simple words, is uplifting the price of the goods when demand gets high and resources are scarce. In this way, you can control the demand without affecting your profit quotient. The main aim of this system of price rationing is to slowly discourage the considerable increase of demand and conserve the resources for a long time. In short, the greater the scarcity of the goods, the higher will be the price and higher will be the rationing of the resource. Consumer psychology clearly states that increased price affects the demand without any doubt, because buyers will spend more time looking for a cheaper deal than spend the money on this one abruptly. This will give the producers enough time to recover from scarcity while using the rationed goods and maintaining their earning from the business.

FUNCTION OF PRICE

When we talk of price mechanism, it is important to note that increase in demand of particular goods will gradually increase its price in the market, thereby affecting the supply curve.

The rationing function of price is associated with the contraction of demand along the demand curve. We can explain this in both raw as well as a technical manner. When we go deep into this topic, price rationing is something which ensures that goods are consumed by buyers who value it the most. Here, in this graph, P1 is the equilibrium price and Q1 is the equilibrium quantity. Somehow, the quantity available is also Q1, and if price is maintained at P1 then demand will exceed the availability of the resource. The buyers who are willing to pay the price equal to P1 are the ones who find the product reliable and compatible for the price they are paying. If the price is increased from P1 to some other amount, then buyers will not consider the product as valuable enough for this newly increased price. Hence, they will not buy the product and they will re-evaluate their needs and uses of this good leading to its elimination because of the higher price. But, at the same time, if a buyer truly wants to buy this good, then they will pay the increased amount. They will not eliminate this product because they truly value it and they truly understand its use in their daily lives. Thus, when we technically look into the concept, it reflects that only those buyers will stick to their needs who value it the most. In summary, we can conclude that rationing function of price guarantees that quantity purchased is equal to the quantity which is available. Also, it ensures that buyers who consume the good are the ones who value it the most and are likely to get maximum satisfaction from the same.



Price mechanism and Trade balance

BALANCE IS USUALLY a term used to explain the maintenance of two opposite factors in any domain. Be it diet, trade, art, or technique, the perfection lies when you try to balance the things in equal amount. In any domain, when you see a downfall, it is probably because of not being able to balance certain factors which are affecting that particular domain. The same thing happens when you are into the business and trade sector. You have to keep track of several things and balance innumerable factors to keep things smooth and stable. Even a single careless mistake can lead to a big loss. One has to analyze each and every consequence to avoid risk in the long run. When we look at the trade sector on a global platform, the most important thing one has to balance is import and export along with the inflow and outflow of capital.

When we generally look at the trade balance or balance of trade, we see that it is related to the difference between the monetary value of import and export taking place in a particular nation over a certain period of time. There are several factors which affect the trade balance, and price mechanism has an equally important role to play in this domain. Just like we have seen in the earlier topics, price mechanism plays the same role in trade at an international level. There are many influencing factors which decide whether the ongoing trade is having positive or negative effect on the economy of a particular nation. For instance, if there is more export as compared to import, then it is called as surplus trade or positive balance of trade. Although surplus trade is seen as a positive factor for the economy of a particular country, the trade deficit or the negative trade is sometimes beneficial for the macro economy of the country. Hence, sometimes government willingly enforces trade deficit to meet macroeconomic goals of the respective country. There is a small exception in this case. Not all the import-export imbalance is negative in nature because in the case of developed countries when import of raw material increases, it is usually for the conversion of raw material into finished products. These finished products are then to be exported to other countries after adding more value to it.

Factors that affect trade balance

Some of the factors which majorly affect the trade balance in any country are given below:

- The first and foremost thing is cost of production when both export and import economy is taken into account separately. This cost includes the cost of land, labor, taxes, incentives, etc. This clearly involves price mechanism because many utilization and allocation of many resources are involved in this process.
- The next major factor is the cost as well as availability of raw materials, intermediate goods, and other inputs which are required by the production company to carry out the process smoothly. One has to manage and coordinate with the central planning authority to ensure that right amount of resources are available at the right location on timely basis.
- There are barriers which are not related to capital or resources. These include environmental, health, and safety standards. If the product or its production process is not fit for the health and environment, then it adversely affects the trade and creates an imbalance. All the quality control tests are to be performed before releasing the product in national or international markets, and it strictly has to pass those tests to get approved for further process.
- The price of the goods which are manufactured for the domestic supply and domestic use also plays a major role. This is the point where price mechanism plays an important role and determines the equilibrium price as well as quantity for a particular goods or commodity.

IMPORTANCE OF PRICE MECHANISM

AFTER LOOKING AT all the above given facts about price mechanism, it is quite relevant to understand the importance of this concept in the economy of any nation. But, in order to understand it in a better way, we will highlight the things in an elaborate manner. There are three main important functions of price mechanism which are extremely important to be understood. Given below are some of the crucial points that will explain why price mechanism is important in the long run.

- **Signaling Function:** In this function, the market price adjusts according to the increase or decrease in the demand and supply of the resource. The prices will determine where the resources are required and where we need to stop supplying the resources. Hence, in simple terms, if the market prices are increasing due to increase in the demand of consumers, it is a clear signal for suppliers to accordingly adjust the production matching with the requirement of consumers.
- **Transmission of preferences:** This is related to signaling function and with the help of this unique system the consumers express their needs and demands. Transmission of preference is all about conveying the change in needs and demands to suppliers so that they can also alter their supplies to the market. The supplier and producer will obviously think about their profit and give a command to their production unit to bring about the changes as per the requirement. In this way, the producer responds to the individual needs of millions of consumers and this is one of the most remarkable importance of price mechanism.
- **Rationing function:** We have already discussed about this topic in prior section and this is also one of the importance of price mechanism. One can easily judge the difference in supply and demand of the resources and adjust the price accordingly to ration the resources without causing any hindrance to the profit quotient.

Therefore, price mechanism is not just a wonderful concept, but a necessity in the market to fulfill the goals of the economy of a respective nation.

MAKE IN INDIA

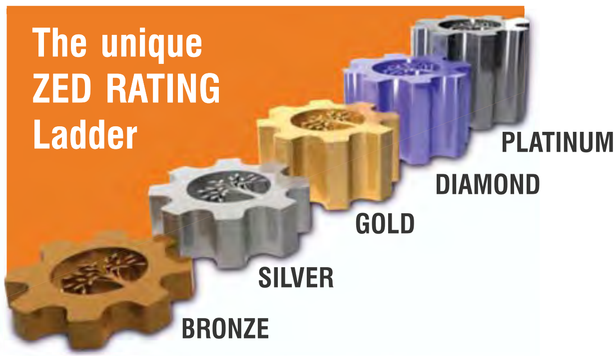
QCI
Quality Council of India

ZED™

ZERO DEFECT • ZERO EFFECT

Certification Scheme

A roadmap to
World-class manufacturing



HIGHLIGHTS

- A scheme by Ministry of MSME, Govt. of India
- Certification on the systems and processes of MSMEs
- Handholding MSMEs towards world class manufacturing
- Special emphasis on MSMEs supplying to Defence Sector
- Direct subsidy to participating MSMEs
- Creating a credible database of MSMEs for OEMS/CPSUs/Foreign Investors under "Make in India initiative"
- Quality Council of India (QCI) to function as the NMIU (National Monitoring and Implementing Unit) of the scheme

"Let's think about making our product which has 'Zero Defect'; so that it does not come back (get rejected) from the world market and 'Zero Effect' so that the manufacturing does not have an adverse effect on our environment"

SHRI NARENDRA MODI
Hon'ble Prime Minister

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CONSUMER BEWARE

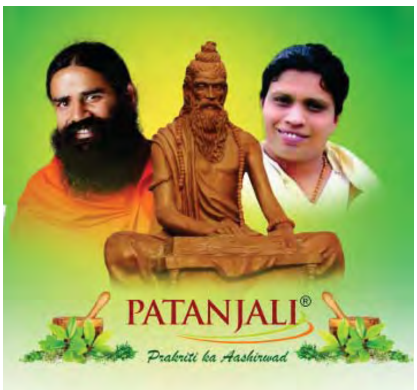
THE ADVERTISING STANDARDS Authority had upheld action against one advertisement from the retailer called Aldi. Like every other firm it claimed that it would be a Money Saver Company and it had organized a campaign where they told the consumer to switch to Aldi rather than the branded shop. They had advertised and broadcasted the advertisement on television picturing that there is a kitchen and inside that there are various products which had other brands in it and were selling it on their own labeled prices.

Advertising standards authority claimed that Aldi can't mislead consumers. Sure they have authority to compare products but without letting any other products identity visible in their ad. Due to this advertisement many had switched to Aldi. The problem with the advertisement was that they can't mislead the consumer by stating whether the product is profitable or not by just selling it at an affordable rate. Plus, there is no such evidence that only their products leads to savings of the consumer.

The most important thing over here is the marketing team and the advertisement agencies must have done a research yet were not well versed with the advertising code before producing it. They should have created the advertisement without misleading the audience by comparing it with other products without surety. Such small issues can create a major loss for the product itself and might disappoint the consumers for lifetime. Companies should know how the consumer interprets a message. The consequences can be very grave, sometimes these misleading ads can directly harm the consumer and can be dangerous for the product seller because their company might also get shut down.

Consumer court is always ready to take action against such companies and even the other seller can take the action if their product has been mis-represented by the other seller. For example the Surf excel advertisement once show cased Tide in their advertisement which not only was noticed by the consumer but the owner too which was misleading. So they compensated by quickly withdrawing and released another advertisement

immediately so that the consumers won't be disappointed. Consumer must check the reviews of the product before buying it and also sellers must see to it that they know their target consumers and know the consumer's needs. Make sure that before buying a product one should look out for other products too. Don't just purchase it because the advertisement was too fancy. Buyers must see to it that they read the terms & conditions given behind the product which will help them out. For example Patanjali products



recently have been highly advertised. The brand ambassador of the advertisement is Ram Dev baba himself and he goes to the farm and makes the product. This might mislead the consumer, even if it says that the product is totally natural it still has got chemicals. Beware of such tactics used by the advertisers they only want to prove their point for their commercial gains.

Advertisement packaging usually increases the expectation of the buyers many a times. A product like Lays for example is full from outside visually but when opened the packet is half in contents. It is the top selling product even though the quality is good the quantity is less. They have improved the quantity many a times by increasing it by 20%. Some products are sometimes over exaggerated such as juices which claim

that they don't add flavor but however when tasted, you will start to know that there is flavor and artificial sweeteners. Claims such as we give you the best chicken by KFC is totally misleading because everyone knows that can't be a true statement.

The buyers sometimes provide you with different quality even if the consumers don't realize that until they reach home and unpack that product. The consumers should keep a note on checking the whole product packaging before buying it, some products claim they have flavor in it and such products shall be safe to buy because they have mentioned everything on their product.

Fair and Lovely is a product that claims that with one use anyone can have a fair skin and this is misleading. When

it was introduced consumers started buying especially those wanting a fairer complexion. Now in such a case it's not only misleading but disappointing as well as it is a claim which the consumer cannot prove. A similar incident took place when Kellogg's had made a new product for all women struggling with obesity, this product didn't make any such difference. Even if it was true partially it mislead and misinformed people about the product. Those who used those beauty products might get skin diseases which are harmful so a product seller must keep all this in mind before selling it.

The production team must have a review section where the criticism must be taken so that the other consumers are aware of such situations. The seller must always initiate a campaign before selling products and use the samples of their product so that the consumers know and

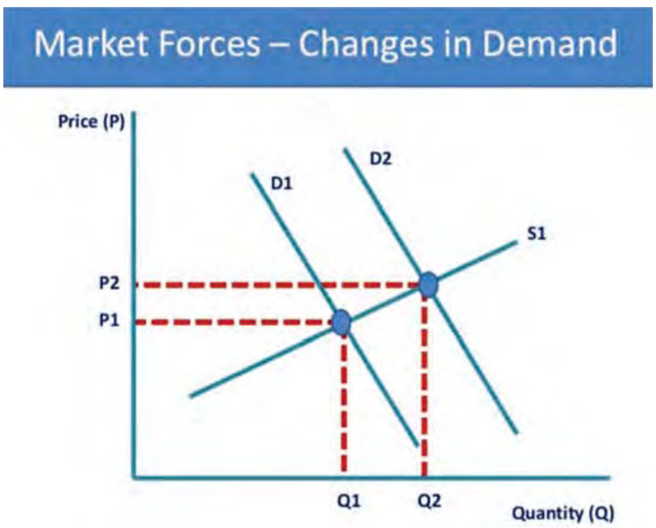
have an idea about it and also give a review on the product. This will help the supplier know what more the product needs. The media must not give any false information. The advertisers must know that the consumers have a right to complain so that they cannot send any misleading message to them about the product. Otherwise they will have to deal with litigation and the product seller might have to pay a penalty plus he/she might have to go to court and prove a point thus bringing disrepute to the brand. Issues shall be raised against the company and the company might face major losses. The consumer mat not be willing to buy the product again. Today's consumers know how and what the advertisements are taking them towards so the supplier must provide accurate information regarding the product so that they are not claimed as illegal.

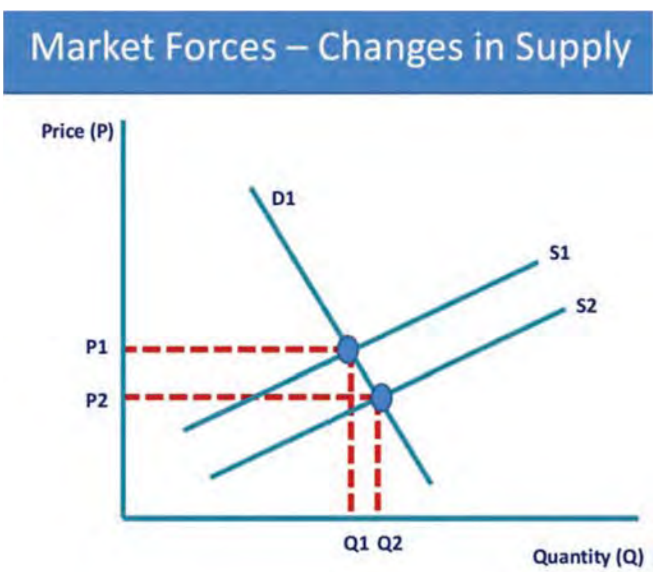
CASE STUDY

1. Conditions Required for Competitive Market in Price Mechanism

A. Consumers have the power to allocate resources, i.e., the monopoly power of sellers does not impact too much on consumer sovereignty

B. No externalities from production or consumption.





C. Full information available to all market participants.

D. Factors of production are occupationally and geographically mobile between different uses.

The breakdown of these assumptions can lead to market failure and inefficiency.

2. Functions of Price Mechanism

a. **Allocate –** Allocating scarce resources among competitive users.

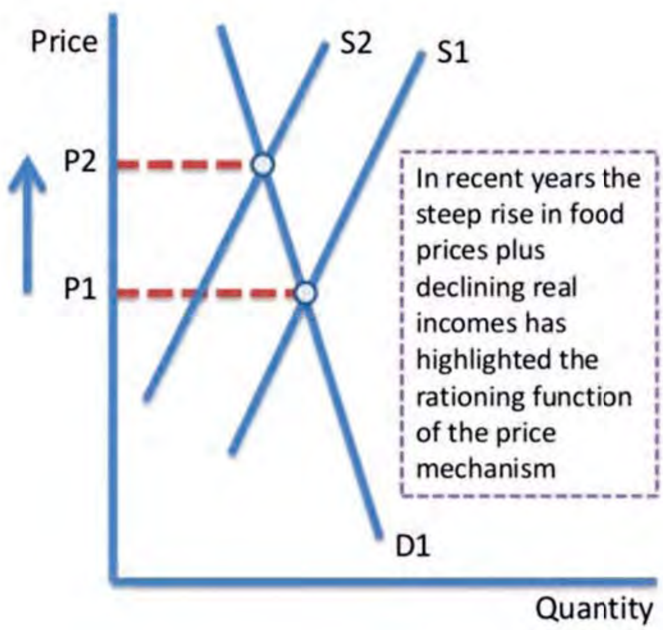
b. **Rationing –** Prices serve to ration scarce resources when market demand outstrips supply.

c. **Signaling –** Prices adjust to demonstrate where resources are required, and where they are not.

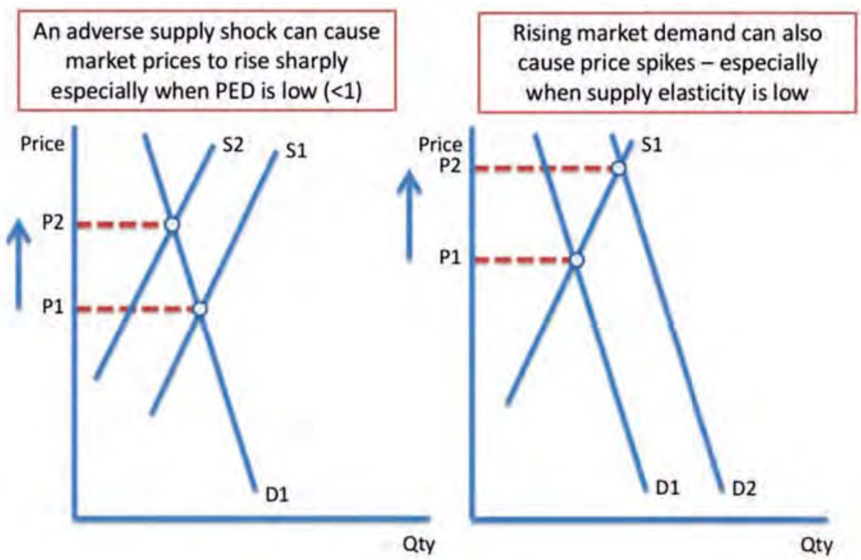
d. **Incentives –** When the price of a product rises, quantity supplied increases as business responds.

3. The Rationing Function

When there is scarcity of a particular product, then the price of it will rise. This would restrict some consumers from buying that product.



4. Causes of Price Volatility



5. Model of Price Mechanism

When changes are large and rapid and in particular when they may need to be reversed again quickly, there are special difficulties in relying solely on the price mechanism for the purpose of bringing them about.

For example- Suppose that it is necessary to increase the manpower in the textile industry by a large percentage in a short period of time. The price mechanism would operate through a rise in the wages of textile workers relatively to other workers.

6. The Case for State Control and Planning

The method of control by the quantitative allocation of resources, quite apart from the real cost of manpower in running the controls is bound to be clumsy, inefficient and wasteful as compared with a properly functioning price system.

For example- The apparently simple question whether one should plan to substitute steel for timber for a certain purpose in building. Is it economic to do so? What are the factors which the official concerned must take into action?

He must first consider the technical possibilities for substituting steel for timber in this particular use. How much more steel is required to replace a given amount of timber, and what will be the effect of the quality of the building? Unfortunately for him, the people who really know about this are not his fellow officials but the technicians in the building industry who have a vested interest in the question and have, let us suppose, set their hearts upon getting timber rather than steel, because at the arbitrary monetary prices fixed for steel and timber, it happens to pay them most that way.

Then there is the question where the extra steel should come from if the substitution in building is made. Should less steel be allocated for the production of cars? If so, can less steel be used for cars?

What on the other hand, should be done with the timber which is saved? Should it go to railway sleepers or to packing cases?

Perhaps, after all, it would be better to produce more steel. If so, what should one give up producing in order to get the additional labour? Coal? Bricks?

One could run through a long list. But this would only shift the problems from steel to other commodities. One would now have to consider all the direct and indirect effects of reduced supplies of coal or bricks or the other commodities selected for reduced production.

Or perhaps one could import less timber and more steel. Here, one may be able to reach a fairly unequivocal answer. For one can judge whether the decreased purchase of timber will save more money than the increased purchase of steel will cost. The firm foundation of the price mechanism at last!

7. The Controlled Use of Money and Price Mechanism

We are facing this dilemma. State planning and intervention seem to be needed to prevent the recurrence of mass unemployment, to ensure a tolerably equitable distribution of income and property, to avoid the anti-social wastes of much of the competitive processes, and to coordinate the vast changes required in our economic structure in the present temporary, but perhaps somewhere prolonged, period of transition from war to peace. On the other hand, when one examines the possibilities of quantitative planning, one cannot be appalled by the prospects of insidious threats to personal freedom and to public morality, of a swollen bureaucracy and of clumsy inefficiencies.

The only way out would appear to be to make a controlled and planned use of the money and pricing systems. Such a solution would combine as much as possible of the decentralized freedoms and peculiar efficiencies of the price mechanism with that extra extension of the field for State planning and control over total money demand, over the distribution of income and property, and over private monopoly which is necessary to avoid the chief evils of the interwar system. And a controlled use of inducements through the mechanism of the money and price system, although for reasons already examined, it could scarcely be relied upon alone to accomplish the rapid and large structural changes which are needed might do much to influence the adjustments required in the present transitional period.

We have ourselves much to gain from the pursuit of this kind of policy. The present time is important, because, in a very special sense, many countries now stand at the parting of the ways- to plan or not to plan, to use the price mechanism or not to use the price mechanism. And the solutions which they now adopt will mould their policies and institutions for many years to come.

Rapid prices rises cannot be allowed to continue indefinitely and at some point, something will be done to stop the price rises. But there will be much demand for goods and services during the inflationary period which is taking place merely because prices are rising, because people are buying goods to hold to sell at a large money profit later. As soon as steps are taken so as to restrict total money demand to stop the rise in prices, all the demand for goods which was taking place merely because prices were rising will, more or less suddenly, cease.

This will bring with it the grave danger that total demand will then decline too much and the vicious spiral of deflation and mass unemployment will be released. A position of rapidly rising prices is, in fact, a very unstable one. History has shown it to be difficult to stop an inflation without causing a deflation. And, to prevent an inflation of prices and incomes from the point of view of making it easier to avoid deflation and unemployment at a later date.

It has become the practice of many countries to deal with an excess of monetary purchasing power by a system of controls over prices and over expenditure which prevent too much money in its search for the too few goods from driving up the price of the latter. This system of suppressed inflation has no doubt avoided many of those particular evils of rapid price increases, which are examined above. But it has brought its own peculiar evils with it.

The control of prices of finished products prevents a price inflation but does not itself reduce the excessive demand for such goods. This excessive demand for final goods on the domestic market continues to exert its pull and sucks goods away from other uses, in particular from export markets and from stock building.

The excessive pull of demand in the home market has undoubtedly been the main factor attracting goods and services away from export markets. If the total internal monetary demand were restricted to correspond to the amount of goods and services which would be available in the home market if we had no excess of imports over exports, producers at home would not be able to find profitable markets at home for all that they produced unless they sold abroad as much as our imports. They would have the strongest motive of profit to divert supplies from the home market and to seek export markets.

When the suction of money demand is so great that everything is pulled into final consumption as soon as it is produced, there is a grave danger that working stocks will be unduly depleted. At every stage there must be adequate stocks of raw materials, of goods in process, of components and of finished products. And stocks are one of the first elements to suffer when an attempt is made to get a quart of final

consumption out of a pint pot of resources. These particular evils- the sucking of goods away from export markets and out of stocks- could be avoided without any reduction in the total amount of monetary purchasing power available on the internal market for the purchase of goods and services, if adequate direct controls were exercised not only over the prices of finished goods but also over the domestic purchase of goods and services.

8. Price Mechanism in Mixed Economy in Relation to Consumer Sovereignty

In a competition prevailing market, the customer is at his discretion of what could bring in welfare for him while selecting a product to purchase and that of his preference in the choice. In a capitalist economy, the consumer has freedom of choice and hence termed as sovereign, king or queen. The consumer is at liberty to buy the product of his choice in any amount of volume. On the preferences of the customer, a producer will sell his goods. This arises to freedom of productivity. The consumers reveal his taste and preferences to the producers through price mechanism. The insistent desire for definite products means the consumers are prepared to pay a huge amount of money. A person who wants to begin an industry will be encouraged by the consumer's preferences, for that specific commodity. Thus the consumer is the sovereign. He decides the price and the manufacturers' produces that merchandise which he prefers more. The more the producers produce the more the profit earned.

Limitations of Consumer's Sovereignty

1. **Unequal income Distribution** - Consumer's independence is restricted by imbalanced income allocation in a capitalist society. Poor consumers have limited choice of products.
2. **Availability of Goods** - Choices are constrained to the goods that are produced and dispersed in the market. The accessibility of goods depends on the availability of resources.

3. **Combined Choice -** The production is based on the choices and preferences of not a single customer but as a whole. Hence the making is made based on the tastes of the majority of the customers. Thus autonomy of customers is not an actuality.
4. **Consumer not rational** - The consumer is not a sensible buyer. He is habitually unaware about the value and eminence of the products obtainable in the market and cannot make a correct choice.
5. **Society's Customs** - The customer's dominion is limited by the common customs of the society in which he lives. His freedom of choice is restricted by the rules and regulations of a society.
6. **Fashions** - The customer's independence is also unfavourably pretentious by the trends in vogue. He would not like to be mocked by his friends and relatives by wearing the dress of his choice.
7. **Standardised Goods** - There is no place for consumer's liberty in a capitalist economy where standardised goods are produced in mass. The consumer has no alternative of his own but to buy them in whatever form, amount and superiority.
8. **Advertisement and Propaganda** - These are in the form of salesmanship, free sampling, complimentary service, door-to-door campaigning, newspaper ads etc. The consumer is influenced by them, and thus it becomes difficult for him to make his own choice.

9. **Monopoly** - The subsistence of monopoly, combines and associates stand in a way of consumer's control. The consumer has to procure the goods produced by the monopolistic at the prices preset by him. There is no other choice for the consumer except to buy the monopolist's goods if he wants to consume them.
10. **Government Restriction** - The government also controls and standardizes the utilization of certain stuff which confines the consumer's sovereignty. The use of intoxicants like wine, opium etc. and injurious drugs is synchronized and even forbidden by the rule. In auxiliary to the control, law and public distribution of indispensable products like kerosene, rice, sugar etc. are also big obstacles in consumer's dominion. Such limits bind the consumer's choice of commodities.
11. **Taxation** - The levying of income tax and product taxes badly influence for consumer's sovereignty. Both are likely to lessen the not reusable income of the consumer with the consequence that his preference of goods is limited.

CASE STUDY

This case study considers how prices are set in the package holiday market had how price discrimination is used as part of the pricing strategies used

Introduction

UK holiday-makers take some 36 million overseas holidays each year. Of these, almost half are "packaged holidays" - where the consumer buys a complete package of accommodation, flight and other extras - all bundled into one price. This is a highly competitive market with a small number of large tour operators (including Thomson Holidays, Airtours, First Choice, JMC) battling hard for market share.

Package holidays were devised partly as a way of achieving high sales volumes and reducing unit costs by allowing tour operators to purchase the different elements (flight, catering, accommodation etc) in bulk, passing some of the savings on to consumers.

Low margins require high asset utilisation

Estimates of tour operating margins vary, but fairly low average figures - of the order of 5% (or around £22 on the typical holiday price of around £450) are widely assumed in the mainstream segment of the market. It should, however, be noted that vertically-integrated holiday operators (where the tour operator also owns an airline and a travel agency) will normally also generate profit from consumers. Accordingly, the gross margins on the total operations of the integrated operators may be larger than those on their tour operation activities alone.

Tour operators need to operate at high levels of capacity utilisation (figures of the order of 95% or more in terms of holidays sold) in order to maintain profitability. Matching capacity and demand, is therefore, critical to profitability, especially since package holidays are perishable goods - a given package loses all its value unless it is sold before its departure date.

Perishable goods markets require highly flexible production and distribution systems so that supply and demand can be closely matched and 'waste' production minimised. But suppliers of package holidays are severely hampered in precisely aligning capacity and demand. They need to 'produce' (i.e. contract for the necessary flights, accommodation etc.) virtually the whole of what they expect to sell a long time before it is 'consumed' (i.e. when the consumer departs for the holiday destination, or at the earliest, when the consumer pays the bulk of the price – usually around 8 weeks before departure).

Long-term management of capacity

Tour operators' capacity plans and the associated contracts with hoteliers and airlines are typically fixed 12-18 months ahead of the holiday season. Some adjustments are possible after this date. However, within about 12 months of departure date, once the booking season has begun (i.e. from about the summer of 2009 for departures in summer 2010) the scope for changes is severely limited. This is due to the inflexibility of many commitments with suppliers and the problems associated with changing dates, flights, hotels etc of customers who have already booked.

Only by contracting for their expected needs well ahead of time, enabling suppliers to plan ahead, can tour operators obtain a sufficiently low price to attract an adequate volume of profitable sales. Tour operators, therefore, need to encourage early bookings. These improve cash-flow – a substantial deposit (usually around£100 per person, equivalent to around 25% of a typical short-haul holiday price) is paid by consumers on booking; the balance is payable two months in advance of departure (except, naturally, for 'late' bookings).

Tour operators also reduce the risk of unsold holidays, and the consequent need for discounting, later on. Adding capacity is easier than reducing it during a season, although in some instances, e.g. where a particular resort is proving especially popular, all suitable accommodation (and/or flights to the relevant airport) will already have been reserved, at least for the peak period. But it is generally difficult for tour operators to 'unwind' their contracts, especially those for air transport, without substantial penalties. The tour operator, accordingly, bears almost all of the risk of any contracted capacity remaining unsold.

The price mechanism

Faced with this limited ability to reduce output in the short-term (i.e. once the brochures are published and the selling season has started), tour operators can, for the most part, only try to match supply and demand via the price mechanism – in other words, by discounting once it becomes clear that sales of their holidays appear unlikely to match the supply that they have contracted.

The fixed costs of tour operation (mainly, the cost of the airline seat and most of the accommodation and catering costs) make up a high proportion of total costs so that relatively high levels of discount can be applied if necessary to clear unsold stock. Reductions of up to 25% off the initial brochure price are available on some 'late' sales – although consumers will often in such cases be required to accept the operator's choice of hotel, or even the resort, according to availability.

Discounting of holidays during this 'lates' part of the selling season is a similar phenomenon to that of 'end of season stock clearance' sales in other retail sectors (e.g. clothing). However, the impact of discounting on 'lates' in a normal season should be seen in the context of the operator's turnover for the season; it is effectively reduced by only about 5% (25% off 25% of holidays sold). Discounts (or equivalent incentives such as 'free child' places or 'free insurance') for early purchase are also offered, but they are much less significant both as to the amount of the reduction (5-10% appears typical) and its impact on costs and turnover. About three-quarters of all package holidays typically are sold at or close to the brochure price.

The fundamental rigidities in the market have important consequences for competition. They make suppliers closely dependent on each other from a strategic, as well as a short-term, viewpoint. In particular, any decision by a tour operator to try to increase market share by increasing capacity (i.e. offering more holidays for sale) will lead to a fall in prices unless competitors reduce their share by an equivalent amount by cutting capacity. ◗

Price determines the production of supply and buyers. The production of goods and services directly effects the economic growth. Let us figure out with other spheres of price in the following

How much to produce?

The first thing is to get the exact ratio of how much to produce and what to produce, there must be right amount and proportionate resources to allocate of total output in the economy. Proper management of goods should be done into different sections so that the resources can be produced properly. Then when the sections are divided there would be allocation of production and the amount to be supplied. The amount of goods to be supplied through preferences and how much the society needs it is according to the research and capital available. The higher the priority of capital on goods the less the consumer will have access to these enormous goods.

Deciding the total output of the economy, the society has to choose the proper combination of capital and the goods available.

How to produce?

The next big task is to know how to produce right after what and how much to produce. Prices are the rewards given by the consumers to the producers for giving them the quantity and quality. For laborers it is in the form of wages, whereas for the land the rent is the reward for the landlords. Rent, interest and profit are the prices paid by the entrepreneur for the services of the productions given to them. Each producers aim is to provide the best service to the consumers along with being the one who provides the affordable prices goods. Sometimes to maintain capital the producers use cheaper resources and market the same. If labor is cheaper than the capital the production has then the laborers will be used more to reach the capital.

The kind of technique used while selecting the type of goods depends on the economic capital. For producing capital amount of goods and large outputs, expensive machines are required. And also, consumer goods and small capital outputs require less expensive machines and use simple techniques.

Market place

Where do the producers and suppliers meet? The market is the place where they exchange goods and depends on the various products to be sold. The consumers also get the goods from the market where the suppliers keep the goods available for the buyers. Examples of markets are as follows : the Housing market such as home owners and potential buyers, Labor market includes employers and workers, Stock market where there are share owners and potential buyers, Foreign exchange market of trading currencies.

There are submarkets too which works under them where as shopkeepers, showrooms, exhibition for houses, various stock markets where people buy shares. Foreign exchange is directly run by the government.

Also when the market is dropping its production then the prices of the goods start to increase and that's why there is lot of fluctuation. Recently onions rate was increased because the market came down.

Secondary markets occur usually when the buyers and sellers decide to prepare to use a second market to sell again those same items that have been purchased before. The best example of the secondary market in the recent times is the tickets for concerts which recently took place of famous singer Justin Bieber although the tickets were supposed to close down they still provided tickets of the gig on the day of the show. Another example is sporting events such as those for IPL tickets.

An auction is a part of price mechanism where the bidders start competing offers for goods amongst them. The minimum bid shall or cannot be set by the supplier, who may choose to keep the price of the product and where to sell it. The highest call of the bidder the more that supplier will be rewarded by the transaction.

Income distribution:

Price mechanism is totally dependent on income distribution in a capitalist economy. In an economy like this consumers and producers are mostly the same people. The consumers provide them money in exchange for the services they provide. The factors of production for consumers sell their services at given prices for the money they have given to producers, then spend the money to buy goods by producers. In the price mechanism system money flows from producers to consumers and then it flows from consumers to producers.

Thus the price mechanism working is through supply and demand in a free economy acts as the principal of organizing the force of production. It determines what to produce and how to produce in the market and the growing economy. The rewards factor the services given to the buyers. It brings out an equivalent distribution of income by distributing resources to be allocated in right directions of the production. It works to rationalize the existing supplies of goods and services, utilizes the economy's resources fully and provides the means for economic growth of the country.

Rationing function

Prices serve to rationalize the scarce resources when the demand from the market outstrips the supply. When there is a shortage in the market, the price goes up, leaving only an option for those with the willingness and ability to pay and purchase the product for their needs, for others it's a difficult thing because they cannot buy goods due to their lower capital and which makes it a huge scarce resource. Be it the demand of tickets for the India and Pakistan match to watch the cricket series or the huge demand for a rare antique such as a painting by the famous artist M. F. Hussain, the market price acts as an opposing device and tries to equate demand with supply while the production house is juggling for the resources. The popularity of auctions came into demand because the means of allocating resources is worth considering for the economic growth and for the increase in market availability and the main motive is to increase the market.

PRICE MECHANISM OF INCENTIVE FUNCTION

An incentive is something that motivates the producer and the consumer to follow the action or to change the behavior of the economy as it is all interrelated to each other. Higher prices provided as an incentive to the producers to supply goods more because they provide the possibility of more revenue increases and so do the profits. The incentive functions when there is a rise in price, it is associated with an extension of supply along the existing supply curve of the production.

Market failure occurs usually when the functions like signaling and incentive of the price mechanism fails to operate automatically leading to a loss of economic growth and huge loss to the society. For example, this happens when the market is failing to take into account the external costs and benefits arising through the production and consumption of the consumers. Consumer preferences for goods and services may be based on imperfect information of the costs and thinks more about benefits of a particular decision to buy and consume a product or not.

In a society where the economic growth is much more important to develop, the decisions like what, how and for whom to produce are not eventually guided by the price mechanism system, it is usually under a capitalist economy. They are made by the planning commission assisted by the various ministries working under them, and also state enterprises. Thus it is the authority that plans the capital and economy of the production.

To the extent that when the price is higher than the market-clearing price immensely increases, it will attract the consumer into the market and raise the markets income. When there is a scarcity of resources of any goods the supplier will immediately call for it so that the customers get a good service because disappointing them can make the production a huge loss. Unfortunately, governments will interfere in that process by putting price limits on the items. Price Controls such as when the price is too high of the product the suppliers usually don't buy it in bulk and thus the quantity decreases that way when the products are sold. So price control can cause a huge drop out in the market value.

The suppliers and the production must also launch such product prices so that everyone can afford to purchase such as oats. It is a cereal which is a foreign product which used to be supplied by the suppliers in bulk and had huge packets when displayed in shelves but now it is completely changed and it also comes in small packaging in a less price for the users. This is based on the assumption that totally depends on the potential of the purchasers' income levels which is not one and the same, which limits the purchasing decision. The price may continue to be bid up and vary until the demand for the resource is reduced and decreased enormously to the point where the demand equals to the supply. All of the scarce resource is thus allocated according to the demand and supply curve.

5 million preventable deaths occur every year

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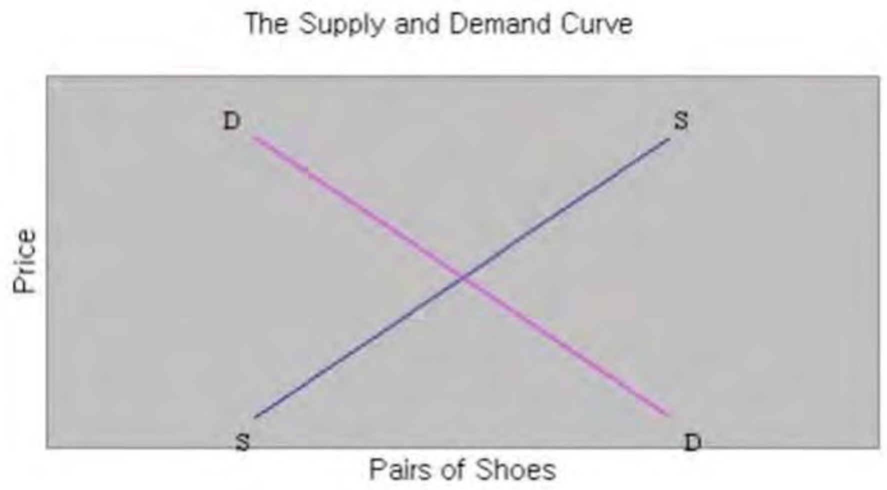
We have already covered the major part of price mechanism and we can certainly say that price mechanism is an indelible part of the economy of any nation. It is an important factor which decides a lot of things about business, profit, loss, and economy. In simple terms, we can say that price mechanism is the backbone of economy which faces straight effects when there is a change in demand and supply culture. Demand and supply chain is an untold custom of business without which it remains an incomplete process. It is obvious that if there is no demand then there will be no use of supplying the goods to market. The supply and demand chain directly affects the system of price determination, also known as pricing methods. This is the most important procedure of production because without determining the price of goods, it is impossible to sell the goods and decide whether the product is fetching sufficient profit or not. Every coin has a bright side and a dark side which are opposite to each other and necessary to strike a balance. The dark side of price mechanism is pricing pollution which is present in the industry like a harmful weed. Pricing pollution is all about how environment affects economy and vice versa. So let us go deep into these topics and explore the concept of price mechanism in a better way.

The role of Price Mechanism in Demand and Supply Chain

The demand and supply chain is the most important predictor of any company's success. As we have already mentioned before, that if there is no demand, there will be no use of supply, and hence, the profit will be at a halt. Thus, before getting into the domain of business, it is important to plan about demand and supply chain and then get to work accordingly. One should analyze and stimulate the capability of the production unit and predict its performance in the long run. The business plans must be optimized in such a manner that under any circumstances, it should beneficial for the business as well as the target audiences. Taking up the order and delivering the commodity to the right place is a crucial part of demand and supply chain because it decides the future of company. Before jumping into the production domain, one should improve their decision making skills so that the flow of finished products is maintained in a hassle free manner. The free economy is strictly based on the demand and supply chain; however, it is a concept which never really exists in a particular nation. Let us look at the role of price mechanism in demand and supply chain.

- We have been reading about this role of price mechanism since the beginning of this topic. The first and foremost role is to decide what should be produced and how much should be produced. The resources are limited and it should be analyzed that where to invest money based on the demand of the society. If the resources are lacking in an area where the demand of the product is high, then it should be allocated immediately from the place where it is in surplus.
- After selecting the nature of the goods to be produced, it is important to decide the quantity of it by carefully reading the exchange culture in the market. In the market of shoes, there is a group of people who have money and want shoes (demand). On the other hand, there is a group of people who have shoes and they want money (suppliers). The aim is to produce the right amount of products in the right place and maintain the equilibrium of demand and supply.
- Another role of price mechanism is to determine how to produce the goods and commodities. The business is all about making profit from the business and satisfying the consumers to maximum extent. Based on the price mechanism, the production unit will decide how much resource to purchase and from where to purchase. The wages of the labor, rent of the area, and taxes determine the technique which has to be used by entrepreneur to produce the goods.



The supply and demand curve should be taken into account while analyzing the role of price mechanism in supply and demand chain. In the market of shoes, there is an inverse relationship between the price of the shoe and quantity in demand. When looked at the concept graphically, it clearly indicates that supply curve (SS) and demand curve (DD) indicates the quantities supplied and demanded and it strictly relies upon price of the commodity. These two curves are helpful in determining how the prices and quantities are fixed in the market.

Price Determination (Pricing Methods)

Price determination or pricing method is an important step involved in the economy without which there is no balance of gain and loss. In simple terms, price determination is a method in which demand and supply is read and analyzed to determine the cost for any particular goods and services. The price determination is not an easy process and it involves good number of steps. The prices are determined in the light of marketing opportunities, competition, and many other valuables which are influencing the pricing factors. We will read about the major steps included in pricing methods.

Market segmentation: This is the first and most basic step where you have to decide a number of factors. This is a process where you decide the type of products which are to be produced or sold. Along with this, you have to decide the cost of its production, and type of customers who will be seeking the products. Apart from this, kind of services to be rendered is also taken into account.

Estimate Demand: The marketers will have to estimate the demand of the product by carefully studying the analytic reports and market news. The prices of competitors are taken into account and potential of the market is decided by introducing different prices of products.

Marketing Mix: The pricing method is not just about cost production, taxes, rents, and other related things. It is a mix of all the marketing strategies used for the promotion, manufacturing, and supplying of the product. It involves product-market strategy, promotion strategy, distributing strategy, and pricing strategy. When all these things are taken into account, it is called as marketing mix. The promotional strategy is something that affects the price of product the most.

Pricing policies: This policy can either be fixed or flexible as per the changing needs and demands of the market. The policy is preferably supposed to be flexible so that pricing can be adopted in accordance with the changing demands from the consumers and changing environment.

Pricing Strategies: This is completely adjustable because it depends on the things which are going on in the market. For example in case the prices of the similar products are cut by the rival companies, change in the economic policies of government, or during the period of recession. These are the situations where there is a need of strategic alertness to bring about change in the prices as early as possible.

Price Structure: It involves the allowance, offers, and discounts which should be given to dealers and suppliers. The final price is determined based on this pricing structure alongside keeping the pricing strategy in mind. This is the final step of price determination and all the production unit has to abide by this method of pricing for a successful business.

Pricing Pollution

Pollution Pricing Reform (PPR) is the process of the adjustment of market rates to incorporate the direct environmental impact on measurable parameters such as dust and gas exhaust from combustion engines etc. This approach is not the same as the general ecologic taxation schemes, where the measurability of the impact is unavailable on short term or direct comparison of the tax affected choice for investment or operation. When a market price neglects the increase in pollution and affection, it results in externality which is a type of market failure. In situations like these the decisions of an individual could lead to environmental harm, as well as to economic disruptions and incompetence.

Some version of a pollution tax or cap-and-trade system is likely to be the best way to attain environmental benefits while minimizing the costs to producers and consumers. It is an alternative form of environmental regulation which is the most efficient in keeping direct government intervention at a minimum level.

Pollution Tax

Pollution taxation charges polluters for the damages their actions cause the environment and others. Such taxes reduce environmental harm in the least costly way, by encouraging changes in behavior that reduce pollution. Energy tax

reform is not about higher taxes. It is about smarter taxes, and moving away from those corporate and income taxes that are most harmful to economic growth. They are more effective than regulation at reducing pollution and can generate significant economic and environmental benefits.

Pollution and property:

Free markets work on the basis of voluntary exchange, so that a trade occurs only if both the customer and the supplier perceive it to be beneficial. And prices are the means by which such perceptions are formed and communicated. The market price signals the information about the strength of consumer demand for a good and about the scarcity of supply for that good, allowing the implicit balancing of supplier's and customer's interests without the need for a managing authority. If the cost of some raw material that is needed in order to produce some particular product goes up, this would directly impact the price of the product being produced by making its price go higher. As a result of the price increase, the consumer demand for the product would go down. These market variations, of which prices are the essential component, are the means by which both scarcities and surpluses are avoided.

The major drawback of price mechanism is that it does not provide complete information and does not necessarily lead to a perfectly efficient distribution of resources. Most importantly, the prices of the products reflect common perceptions, even when those perceptions are biased and are based on incorrect information. The price mechanism also falls short when a this type of a voluntary transaction between two parties impacts a third party, producing some sort of harm to an innocent spectator. This is the problem of externality that has been mentioned above, and it is why pollution and environmental degradation are one of the major challenges to the free-market system.

The failure of pricing is due to the lack of clear property rights for the environmental welfare. If the clean air in question is owned by a third party exposed to air pollution, then any action that involved contaminating the air would require his approval, which would be granted only if the one who is polluting the air compensated him for the damage caused to innocent's property. This would then establish a price for the environmental good, and the free-market system could account for its value to everyone involved. Irrespective to the fact if the firm paid for the use of the air or the person exposed to the pollution paid the polluter to cut the emissions, the simple establishment of property rights over the air would allow a price to be set for the environmental good. This, consecutively, would meet the important prerequisite for the free market to bring about ideal amounts of both production and environmental safety.

Government Perspective and Interventions

Sometimes, in a totally free market economic system, mainly scarce resources are allocated through the price mechanism. Price mechanism is basically where all the preferences and spending decisions of many of the consumers in the market and all supply decisions of many different businesses come together to determine the equilibrium prices. The free market basically works through all the price signals. Especially, when the demand is high, all the potential profits from all the supplying to any market rises, thereby leading to an expansion in the supply mainly in order to meet rising demand from consumers.

Day by day, the free market mechanism remains an extremely powerful device for determining how the resources are allocated among all the competing ends. Sometimes, the government may choose to intervene in the price mechanism on a large basis, mainly on the grounds of wanting to change the pre-allocation of all the resources and basically achieve what they mostly perceive to be a major improvement in economic and social welfare of the society. Every single government of every political constituency help intervene in the economy, mainly in order to influence the allocation of scarce resources among the competing uses. Their objective in such a scenario is to ensure that every individual gets an access to the essential commodities and services by maintaining the reasonability of their prices

Policy intervention

There are many reasons behind policy intervention. The major reasons are basically to correct for any market failure, to achieve a more equitable distribution of all the income and wealth and also to improve the overall economic performance. The government may sometimes intervene the market by using the price control, tax and subsidy issues. The governments may also intervene in the markets to promote general economic fairness. They may sometimes intervene in the markets to promote other goals such as national unity and advancement. There are certain important terms to remember while considering price mechanisms.

- **Inefficient Market:**

An inefficient market is an economy where social optimality is not achieved and the resources are not optimally allocated. The governments intervene in the markets to address this inefficiency. In an optimally efficient market, the resources are perfectly allocated to those that need it and in the amounts they need it in. In inefficient markets, the case is different, some may have too much of a resource while others do not have enough.

- **Price ceiling**

A price ceiling basically occurs when the government puts a legal limit on how high the price of a product can go despite having so many obstacles to face. In order for a price ceiling to be really effective, it has to be set below the natural market equilibrium. This way the product or service can be accessed by anyone who has the ability to afford it. The government keeping the overall welfare of the citizens in mind tries to impose certain rules or policies, subsidizing the product is the most popular method. There are many other ways in which the governments all over the world intervene to handle such scenarios of high demand.

- **Lottery**

The lottery is one of the most efficient ways to distribute a product for which there is a massive shortage in order to draw names out of a hat. In some states there is an extremely high demand in order to be able to hunt for moose, but the government has also limited the amount of permits it gives out per year. It is very often that these states have a lottery and if users are lucky enough to get drawn, then they can try their luck at finding and shooting a moose during the best season. Although, in this case the citizen purely relies on his luck to get a chance, it is still followed and tried every year. It might seem unfair to most of them who still haven't had a chance to win but somehow people are still convinced to try one more time each year.

- **Price floor:**

A price floor is basically the lowest legal price at which a commodity can be sold. Price floors are mainly used by the government in order to prevent the prices from being too low. The most common price floor is the most minimum wage, which is the minimum price that can be covered for any kind of labor. Price floors are also used often in the agriculture sector, mainly in order to try and protect farmers.

The Black Market

The black market is the venue where all the transactions and businesses take place outside the government authorized channels. These dealings usually occur under the table and this allows them to skip the government levied taxes and price controls. It is completely illegal and is considered as a federal or criminal offence based on the product that is being bought or exchanged. The black market is therefore the venue where controlled and government regulated products are illegitimately traded. It has the power to influence the economy and bring it down because they are shadow markets where these economic activities are not recorded thereby allowing the individual to skip taxes. The black market is basically for all those lucky users who want to get some of the short supply, and they are proven to be often better off selling what they have obtained from all the sellers that will mainly get more benefit out of it.

Impact of black market:

In some of the major cities there have been many ceilings put on the apartment rent itself. While the demand for apartments goes on increasing, the rent however remains the same. On the other hand, when some of the renters are ready to move, they basically sublet their apartments instead of ending their contracts on the whole. Sometimes the government would allow all the consumers that were already accustomed to continue consuming. This would be extremely hard to do since, after the price ceiling is utilized, there will be a lot more people claiming that they have consumed in the past. Also, the quantity supplied is eventually decreased which will eventually leave some of the historical consumers wanting more.

Surplus

When there is a very minute quantity which is demanded than the quantity supplied. This is basically called a surplus. If the surplus is allowed to be in the market, then the price would eventually drop way below the equilibrium point. In order to prevent this, the government must involve itself in the whole process. They can also somehow strictly enforce the price floor and let all the surplus go to a waste. This means that all the major suppliers that are able to sell their goods are much better off than those who will not be able to sell their goods. The government can mainly control basically how much is being produced. In order to prevent a lot of suppliers from producing goods and products, the government can give out a lot of production rights or even pay people not to produce goods. Giving out production rights will eventually lead to lobbying for all the lucrative rights or even bribery for that matter. They can also subsidize the consumption of goods and products in order to get all the demanders to purchase most of the surplus goods and items, and the government can also eventually pay a part of the costs. This tends to get more expensive, really fast.

Subsidy

A subsidy is a benefit given by the government to groups or individuals, generally in monetary form as a cash payment or a tax reduction. It is typically given to relieve the individual from some kind of burden and is often considered to be in the overall interest of the public or a public welfare act. A subsidy is the most basic form of financial assistance that is paid to a business or economic sector. Majority of the subsidies that are made by the government for all the producers or distributors in an industry.

This is done in order to mainly prevent the decline of that industry or even prevent an increase in the prices of its products or simply to encourage them to hire more manual labour. One of the biggest advantages of subsidy is that they result in much lower prices for the consumer. Although the government implements the price ceiling in order to set the minimum price, the subsidies also have their value in the market. The process of Price ceiling mainly helps consumers buy the goods which they need, and it is also extremely helpful for the consumers to get all the goods. Whenever this occurs in such kind of a situation, the governments adopt to give necessary subsidies to the producers, so that the producers will be able to satisfy users on the revenue and continue produce the product and consumer will allow buying it in the price. On the other hand, when the government gives subsidies to users, a national fee will then have to be paid from the tax revenues and therefore result in a higher tax.

Price mechanism

A price mechanism affects every kind of economic situation in the long term. A price mechanism is basically a system by which the basic allocation of resources and the distribution of goods and services are also made on the basis of relative market price. Setting the price ceiling and price floor is basically to ensure that producers and consumers would allow users to either earn profits or buy the goods. Even though, the setting price control would sometime end up making various kind of market distortions, and

In order to prevent a lot of suppliers from producing goods and products, the government can give out a lot of production rights or even pay people not to produce goods. Giving out production rights will eventually lead to lobbying for all the lucrative rights or even bribery for that matter.

the government can analyze the market and also utilize the price control extremely effectively. While setting the price control, the government must consider strengthening the complete economic management in order to reduce the problem as common as the black market. Tax is always an important income of every country. So, the government encourages charging tax on every product and all of the services.

If the government prevents their country to purchase some unhealthy products, they may end up charging higher tax on it. For other goods and services, government should charge lower tax on it because lower tax will have higher economic grow. Government intervention as the buyer is mainly intended to protect all the producers and government intervention as the seller which is mainly intended to protect all the consumers. Maximum price fixing, are mainly intended to protect the consumer society connect, mainly with the high price. Maximum pricing should be always below the market price, but it is not necessary that all the work will be completed. The occurrence of surplus demand, the existence of a relatively fair system of rationing, black market and the government's actions in order to combat the black market. Minimum price fixing on the other hand, are basically intended to protect the producers connect.

The major goal of the government is to ensure the availability and accessibility of the products in addition to the balancing of the supply and demand fluctuations. The policies issued by the government to intervene in the general market is to avoid the market to turn into an inefficient market. By fixing the price ceiling and price floor, the businesses are forced to keep the prices under that bracket allowing greater affordability, which thereby reduces the spiking of prices due to high demand and low supply. In addition to all this, the government also needs to keep an eye on the activities and transactions in the black market which might impact the overall market economy indirectly. Also, the payment of the taxes by the individuals needs to be ensured. When the consumers are generally taxed then the purchasing power of the consumer is eventually reduced, the total demand is reduced, the demand curve ends up shifting to the left down, the price eventually gets a level down if there was a division of the tax burden that was passed over onto the manufacturer. Meanwhile, whenever consumers are given subsidies in general this tends to occur, and eventually its purchasing power also eventually increases, the consumer demand increases, prices eventually also rise, and also the distribution of subsidies.

सत्यमेव जयते

Department of Pharmaceuticals
Ministry of Chemicals & Fertilizers
Government of India

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> \- Narendra Modi

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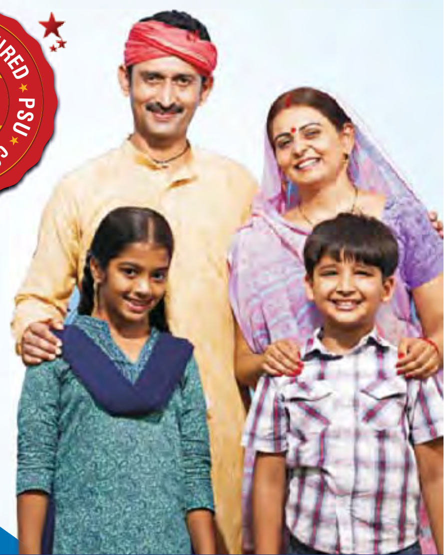

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“Consumer Rights Are Our Fundamental Rights, IT is our Duty to ensure we are not shortchanged”

ONGC may save Rs 800cr from kerosene price hike

On March 2016, the Government cuts gas price to $3.06/mmBtu and boost for fertilizer because the move will benefit fertilizer, power and steel companies. This reduction will ease their working capital burden.

Below is the verbatim transcript of RS Sharma's interview with Latha Venkatesh and Sonia Shenoy on CNBC-TV18.

Q Before we start the conversation about the issues of prices in the market, can you please tell us what price mechanism is?

Q In economics, price mechanism is the manner in which the prices of goods or services affect the supply and demand of goods and services. For example, if the price of a particular car is high, then the supply will reduce as people will stop buying that car. But, on the other hand, if the price of the same car falls, then the supply will increase as people would want to buy a car for less price.

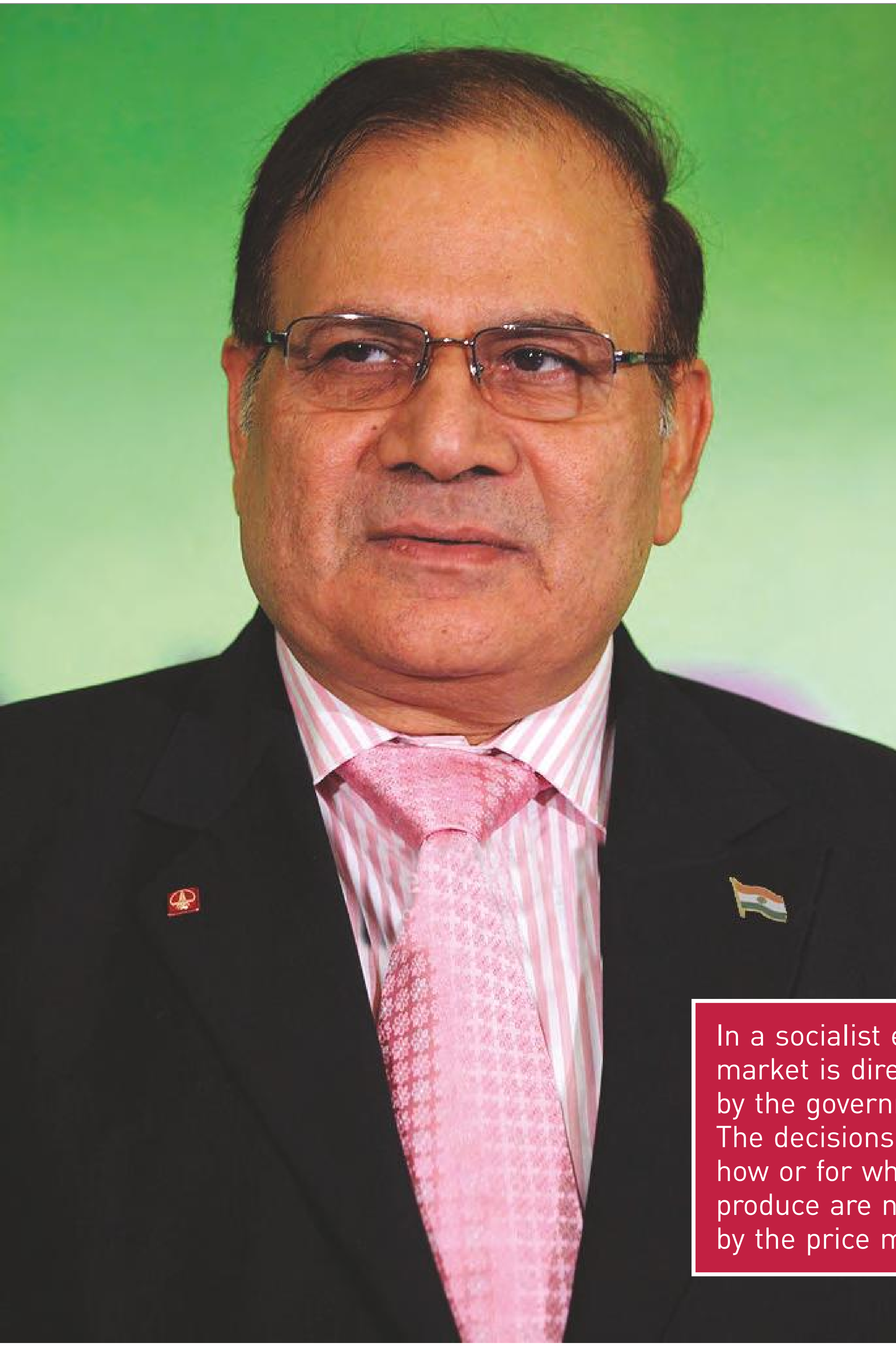
Now, when this scenario happens, another problem rises up. As the production and manufacturing limits are limited; or we can say, as the natural resources are limited, the unlimited needs of people can't be satisfied at once. When the prices of a particular product fall, a lot of people would want to buy it. And when this happens, the limited stocks get replenished and to maintain that situation, the prices slowly rise to maintain a balance in the market.

All of these studies cover up the subject of price mechanism.

Q How does price mechanism work in the socialist economy?

In a socialist economy, the market is directly controlled by the government. The decisions of what, how or for whom to produce are not guided by the price mechanism. These decisions are made by the central planning board assisted by the various ministries, industries and state enterprises. Thus, it is the central planning board that performs the functions in the market.

There are government schemes and plans meant for the public wellbeing and the decisions of what and how to produce are based on objective and priorities in the plan. The central



RS Sharma
Former Chairman and Managing Director

In a socialist economy, the market is directly controlled by the government. The decisions of what, how or for whom to produce are not guided by the price mechanism.

planning authorities decide if more cars are to be produced instead of bikes, if more houses are to be made instead of hotels or more amount of particular food is the be processed than other. They even fix the price in the market and nothing can change it without the government's consent.

Here the disadvantage is, administered prices are set by the central authority without calculating the actual prices required for production or manufacturing. The decision of how to produce is also taken by the government. People have the freedom to buy commodities according to their needs and income.

Q The announcement has come, administered price mechanism (APM) gas price has been cut to USD 3.60 per mmBtu from USD 3.8 per mmBtu. The impact for ONGC will be brutal?

Yes, let me clarify one thing. It is not only APM gas price, even non-APM gas price as of now gets reduced to this level. So including the gas production coming from the Reliance Industries Ltd (RIL), from the Cairn, this is the price APM as well as non-APM gas as of now. It was expected that it will be about USD 3.3 per mmBtu to USD 3.25 per mmBtu but it has come quite low.

Q Now what would be the impact be on ONGC itself, a company that you know so well and then if you can tell us the impact on downstream?

Firstly impact on ONGC because all the existing production coming from onshore areas including the west coast. So over there, this will still be viable to produce because in case of gas, the operating cost is very minimal. So that will be okay. Issue was always that what happens to the discoveries made in the east coast and the price for that and for this the government has announced new mechanism for the pricing. So right now, of course it was expected that prices are going to be lower but through my understanding, they are even lower than what market was expecting.

Downstream, so far GAIL is concerned, I don't think GAIL will have a negative impact from that. For the consumers, it is a welcome step for the industry, the fertilisers and all will welcome this.

Q Is this some way to quantify what the approximate revenue loss could be for a company like ONGC because of the cut in gas prices? I was reading a report by a consultancy, which suggested that to the tune of around Rs 2,500 crore could be the loss on revenues or the hit on revenues because of the cut in gas prices. Is that a logical estimate?

Yes, you are right that I don't have a precise numbers with me right now but ballpark number would be that Rs 2,000-2,500 crore that we have negative impact on the revenue for ONGC.

Q What about fertiliser companies and others who get the gas, will there be at least easier working capital because I assume it is for them only a pass-through?

Yes.

Q So steel companies, power companies would benefit?

Sure, even though it is a pass-through, as it is the prices are high. You know how much problem power companies are having with recoveries from the state.

Q Will there be any impact on the overall investments into the oil and gas sector or have investors already prepared themselves for a sort of a low price regime over the next couple of years?

The current reduction was expected. It is not a shocker for the industry but to my mind, expectation was that it will be around USD 3.25 per mmBtu but it came around USD 3.06 per mmBtu. New investments that the government has announced uniform licensing policy under that the companies will have freedom to market the gas. So they will not be forced to supply to power or fertiliser at the depressed prices or controlled prices. So that is a very categorical and positive statement that has come from the government. So I feel that the new investment will not be impacted by this.

Q Obviously the guys in the east coast are not getting the gas, there aren't enough pipelines, so the power companies

As the natural resources are limited, the unlimited needs of people can't be satisfied at once. When the prices of a particular product fall, a lot of people would want to buy it. And when this happens, the limited stocks get replenished and to maintain that situation, the prices slowly rise to maintain a balance in the market.

still don't benefit. Indian Oil Corporation (IOC) is planning to put up an liquefied natural gas (LNG) terminal in the east coast, any idea when it is likely to be ready?

To tell you that there are as of now about 17-18 projects coming about east coast and west coast where the announcement will come for the LNG terminals and because everybody knows that we have shortage of oil and gas, so in future there is going to be a lot of import of this LNG. So when this IOC project will come up, I am not able to see but surely after the announcement is done, it will be four-five years.

Q What are the other effects of price mechanism in the long run?

A price mechanism effects every economic situation in the long term. Another example of the effects of price mechanism in the long run is the fuel issue. Today, the demand for fuel is usually high. So, it is also possible that we might face a time when the prices of fuel will be high to maintain the high demands in the market.

When this happens, and the prices of fuel rise, the demand for fuel will decrease. The demand won't decrease because the prices are high and people will wait till it doesn't go down. Instead, people will search for other alternatives like electric cars or bio-diesel fuel.

A price mechanism is a system by which the allocation of resources and distribution of goods and services are made on the basis of relative market price.

Q Can you tell us about the effects of price mechanism in relation to the food crisis that is crippling all around the world?

There is a global food crisis we all are facing today. It is also a serious issue that needs serious attention and the United Nations are working very hard to look unto this matter. As I said, under price mechanism, if there is an increase in demand then the prices will go higher, causing a movement on the supply curve.

Food prices are soaring today. There is an increase in demand for food from richer economies, poor harvest, bad weather, rise in fuel prices and several other factors that decrease the supply of food and in turn, increase its demand due to high population. Naturally, the prices rise when the supply goes down.

When prices of food products rise, this creates an imbalance in the economy as the poorer nations cannot afford to buy food with such higher prices. This leads to malnutrition, poor living conditions and the development of the nation is hindered as people of that nation do not get proper food to eat. These poorer nations then become vulnerable and it's difficult for them to rise among others as they get poorer day by day.

Thank you for giving all these valuable information. I am sure our readers will get to learn about the workings in the economy after reading the information you gave. That's all for today and I would thank you again for taking out your valuable time to give this interview.

PRICE DISCRIMINATION

IN THE MARKET economy with the price at its crux, the features of the product, quality, quantity, etc. encapsulate their impact into this single most fundamental unit. Under ideal conditions, we would have a market with perfect competition where the market consists of identical products with the firm having absolutely no control over its prices and the market allows the free entry and exit of the sellers. This however, is a theoretical concept and is used as a benchmark to which real life markets are compared. Imperfect competition is a more realistic and practical concept which refers to a market with heterogeneous products being sold by numerous sellers. This usually allows more types of buyers to be attracted to buy products thereby producing more profits. There are four kinds of imperfect markets namely- monopoly (only one seller controls the entire market), oligopoly (few sellers of goods), monopolistic competition (many sellers with different products) and monopsony (only one buyer of a product). Some of these markets are tough to enter but easy to exit. Now with the markets being so different the flow of money and the fixing of the prices is going to be different as well. Let us discuss some of the contributing mechanisms into the fluctuations of these prices and how they are efficiently managed.

Price discrimination and design mechanism

In order to compete with the numerous firms in the same market, it is one of the competitive measure taken by the established firms in order to generate profits from the supply and demand differences from the customer. Price discrimination is a pricing strategy that takes place when a business or seller changes the prices of the same or almost the same product in an attempt to extract higher profit levels. The prices are increased to the maximum extent up to which the consumer is willing to pay, thereby eliminating excessive demands in the market by the consumer. By limiting the consumer base for a particular product, it could draw higher profits by demanding a higher price which the consumer would be ready to pay. This however, poses some challenges in determining what the exact price is for every buyer. For the price discrimination to succeed, the businesses must take a good look at their consumer base, their needs, and other contributing factors to making a purchase. There are three major types of price distributions:

First degree price discrimination:

In an ideal market, the consumer surplus is eliminated by through the first degree price discrimination. This type of price discrimination takes place when the businesses can pin point the price each of the customer is willing to pay for a specific product or service and then that good or service is sold at that determined price.

The firm selling that good can use data mining to gather information about each consumer's purchase habits, income, budget, and other facts to help towards understanding the buyer better. This is very time-consuming and poses a lot of challenges to many businesses. But if they succeed in identifying the right prices, the seller can get the highest amount of available profit for each sale that would be made.

Second degree price discrimination

Unlike in the first degree price discrimination, in this pricing strategy the ability and resources to gather information about the potential buyer is not present. They alternatively choose to produce goods in quantity rather than focusing on quantity for a specific class of consumers. These companies fix the prices of products or services bases on the preferences of various groups of customers.

Usually, the second degree price discrimination applies quantity discounts so that the customers can make purchases in bulk and receive special offers that are not given for single unit purchases. They often attract customers through coupons, gift cards and loyalty points. Warehouse retailers use this strategy the most. This strategy does not eliminate the consumer surplus but allows the firm to expand their consumer base thereby increasing the profit margins.

Third Degree Price Discrimination:

This strategy is applied when firms fix the prices of their products and services differently based on the different types of consumer base they have. It can be a firm preferred by students, military personnel, senior citizens etc. The third degree price discrimination helps the firms in understanding a spectrum of preferences of the consumers more easily than the buying preferences of each consumer. This also provides a way to control the consumer surplus by sticking to the price elasticity of demand of specific consumer bases.

This type of pricing technique is usually seen in movie theatre ticket sales, restaurant offers etc. The consumers who are unable or unwilling to buy a product due to their affordability issues are dealt by this pricing strategy, thereby increasing their profit margins.

Optimal reverse pricing mechanism

Reverse pricing is market mechanism surfacing under which a consumer's bid for a specific service or good is sold on that particular demanded price when the bid exceeds the seller's hidden acceptance threshold price value, which indirectly depends on the seller's marginal cost. This strategy is based on the customer's bid and once the seller finds the price optimal to gain product, the price is accepted by both the parties and the product is then delivered to the customer. Reverse pricing is popular in markets with unexpected demand graphs and supply fluctuations in industries with volatile prices or demand such as the travel industry.

The essence of reverse pricing is essentially reversing the order of the steps involved in a regular purchase. In the usual

scenarios, the seller sets a certain price and the consumer buys it at that rate. In reverse pricing mechanism the prices are set by the consumer and the seller sells the product once he notices a marginal profit. The seller assumes a base price and waits for the consumer to bid price exceeding that. This process allows the seller to use a bid-acceptance rule only when the bids are profitable. The consumer also needs to make sure if he wants the buyer to know about the current bid-acceptance level.

Fair Price shop:

A fair price shop is a shop that has been issued a license to distribute essential commodities by the government. This is to make sure that every essential commodity is being sold at an affordable rate to certain low income communities. It sells goods such as food staples, fuels etc. at subsidized rates to ensure everybody has access to the basic survival needs. The items sold at these shops are fairly inexpensive but are of average quality.

In India, this is known as Public Distribution System which is an Indian food security system. Under the government of India, the Ministry of Consumer Affairs, food and public distribution ensure the distribution of subsidized food and non-food products to the India's poor. The state government can fix an amount as the fair price shop owner's margin, which could be reviewed at periodic intervals to ensure the sustained viability of the fair price shop operations. Fair price shops are forced to make the information about the opening and closing stock, sample quality of the food grains being sold, retail price details etc. to be disclosed to the authorities. The accounts are monitored and audited at the end of every month by a designated government authority along with the local authorities. Ration cards or pink cards are given to the consumers to keep a log of the products purchased every month and to keep a record of the poverty stricken consumer base that is making use of these fair price shops.

This system has although been under scrutiny and criticism for its urban bias and their inability to serve all the poor sections effectively. In addition to this, there are growing instances of the buyers getting low quality food grains from the ration shops. Illicit fair price shop owners have created a large number of fake cards to sell these food grains in the open market at higher rates and make great profits. There is no proper determination as to who is eligible for these services since it is different in each state. This makes the system highly flawed and irregular.

These are some of the multitude of concepts that involved price mechanism making it an essential part of the economic markets. The determination and discrimination of price is directly dependent on the demand, supply, consumer and producer along with the market in which the product is being sold.

DART
DETECT ADULTERATION WITH RAPID TEST

FOOD IS ESSENTIAL for sustenance and has an equal significance in everyone's life irrespective of their socio-economic or demographic background. Food adulteration is a process in which the quality of food is lowered either by the addition of inferior quality material or by extraction of valuable ingredient. Adulteration of food not only deceives the consumer but also causes risk to their health.

In order to educate the consumers on food adulteration and the importance of food testing, Food Safety and Standards Authority of India (FSSAI) recently brought out a manual entitled **"Detect Adulteration with Rapid Test (DART)".** DART is a compilation of some common quick tests in order to detect common adulterants such as non permitted artificial and toxic colours, extraneous matters deliberately added to food in order to reap economical benefits.

This user-friendly manual describes a total of 40 tests categorised as per the specific food categories -

- Milk and Milk products
- Oils and Fats
- Sugars and Confectionary
- Food grains and its products
- Spices and condiments
- Miscellaneous

The tests are lucidly described with the relevant photographs to depict the actual visual results in case of both unadulterated and adulterated food samples. This handbook will enable the consumers to rule out any doubt regarding the quality of food by testing it themselves at their homes.

You can download your free copy of DART booklet from the FSSAI website www.fssai.gov.in

Find out the related videos on our youtube channel - Lab test of Kitchen: Check out if the products you are using are adulterated (https://www.youtube.com/watch?v=iZkZP8rH2xo)

fssai

सत्यमेव जयते

FOOD SAFETY AND STANDARDS AUTHORITY OF INDIA

Inspiring Trust, Assuring Safe & Nutritious Food

Every aspect and every concept has different types and faces; so is the case with price mechanism. This is a system where you immediately have to respond to the shortage as well as surpluses of goods and commodities. In either of the two cases, one should be ready to alter the market mechanism. Price mechanism may appear like any other casual system in nation's economy which benefits the government in many ways. But are we sure about the economy itself? Is there a uniform economic system in any country? Well, if you carefully examine all the facts, it will show you a different image of the economic system. Implementing the price mechanism in response to the change in demand and supply of the market is not as easy as a smooth piece of cake.

There are a lot of factors involved in this process and ignoring them will not fetch any benefit to the country. The shortages lead to increase in price and surpluses lead to decrease in price. However, it is made sure that there is no huge loss to production unit, suppliers, and buyers. In order to check any type of discrepancy, we have read that controlled price mechanism comes into play. This is where a government interferes in the system to ensure that neither resources nor consumers are exploited in any way. The economy of any nation faces a range of crests and troughs and it gets through all the imbalances with the help of these wonderful back-up plans introduced by qualified officials. The prices continue to rise until the shortage of the good is eliminated. Similarly, the prices continue to fall until the surplus of the good is eliminated. In this current section, we will let you know about the role played by price mechanism in different types of economy.

Price Mechanism and Mixed Economy

Mixed economy is an economic system which includes both socialism and capitalism. It is a system where private property and asset is protected and the private sector is given some amount of economic freedom to use the capital as per their wish. But, there is also intervention from government to monitor and check the on-going economic activities, so that social goals are achieved alongside the economic goals of the nation. It is often argued that free market economy is way better than the mixed one, but interference of government ensures that there is no exploitation of capital freedom which is given to private sector. In simple terms, the mixed economy is healthy for nation as per practical application because both public as well as private sectors are given a chance to flourish. However, they compete for the same resources, but they do not create a hindrance in the growth of each other's market. The monitoring done by government makes sure that things are carried out in a peaceful manner and there is no competitive exclusion in the economic system of the country. The work of government is to monitor the profit of both sectors and nationalize the companies which are deemed impediments to the public goods and commodities. The interference of government may include protection of public distribution goods, agricultural sector, and resources required by government production units. Given below are some points that will explain the role of price mechanism in mixed economy in a clear manner.

- In such a system where private sector is competing with public sector for the limited amount of resource available to them, the price mechanism decides what to produce and in what quantity. The nature of the goods and commodities will also be decided by the market mechanism.
- While the central planning authority of a country decides the price and nature of the goods to be produced, the public sector has its monopoly in the market. All the goods will be produced by analyzing the preference of the consumers and the prices will be fixed based on anticipation of affordability of consumers. The profit price policy laid down by the central planning authority will be considered while fixing the price of the good.
- The public utilities services such as water, railways, electricity, gas, and communication will be decided by the state government on the basis of no profit – no loss policy. The how and what factors of goods production will be done partly by state and partly by price mechanism. In private sector, the profit motive decides what to produce and how much to produce. Also, there is an intervention from central planning authority that influences the working of market mechanism.
- As there is monopoly from public sector, the state guides private sector on what techniques to adopt based on the preference of consumers and their income. On the guidelines of state, the private sector can reduce the cost and maximize the profit. It is responsibility of the state to decide where to use capital intensive technique and labor intensive technique, and ultimately the private sector will adhere to the rules laid by them.
- As far as the target consumers are concerned, in private sector it is decided by both market mechanism

All the goods will be produced by analyzing the preference of the consumers and the prices will be fixed based on anticipation of affordability of consumers. The profit price policy laid down by the central planning authority will be considered while fixing the price of the good.

and central planning authority. Also, the allocation of resources is not entirely left because mixed economy maintains the social justice along with seeking the profit from business. Whereas, in public sector the state government decides for whom to produce by analyzing the overall preference of the consumers.

Price Mechanism and Free Economy

Free market economy is a type of economy where there is hardly any intervention from the side of government. In some cases the government poses few restrictions to keep the things going in a streamlined

manner, but in most of the cases there is no interference from government. The market and business is solely dependent on the supply and demand of a particular good or commodity. The participants of the business such as consumers, suppliers, producers, and plant managers decide what to produce, how to produce, when to produce, how much to produce, and for whom to produce. When practically analyzed, a free market economy does not exist because there is always a small amount of rules and regulations from the government of respective country. They wish to regulate the functions as per their calculation and expectation from various industries.

- The first function of price mechanism in free economy is to decide what to produce and how much should be produced. If necessary, allocation of resources is also done based on the demand and supply in particular place.
- If one society does not prefer a type of product, whereas the other society prefers, then production will take place in accordance with the preference of particular product.
- Another role played by price mechanism is when we ask how to produce. The cost of production comprises of the rent, interest, wage, and profit. The entrepreneur is supposed to decide the price of production and what means they will be using for the same. If the profit from the outcome is not up to the mark, then the production cost is likely to go down by making certain changes or modifications in the whole plan.
- In free economy, the price mechanism is mainly about flow of the good from producers to consumers, and then again from consumers to producers. The consumer sells its service to producers, and the money earned is used to buy the products manufactured by the producers. The process is more or less cyclic in nature.

Price Mechanism and Socialistic Economy

A socialist economy is the one where government controls and regulates the economic system to make sure that equal social opportunity is given to the people of respective nation. In socialist economy

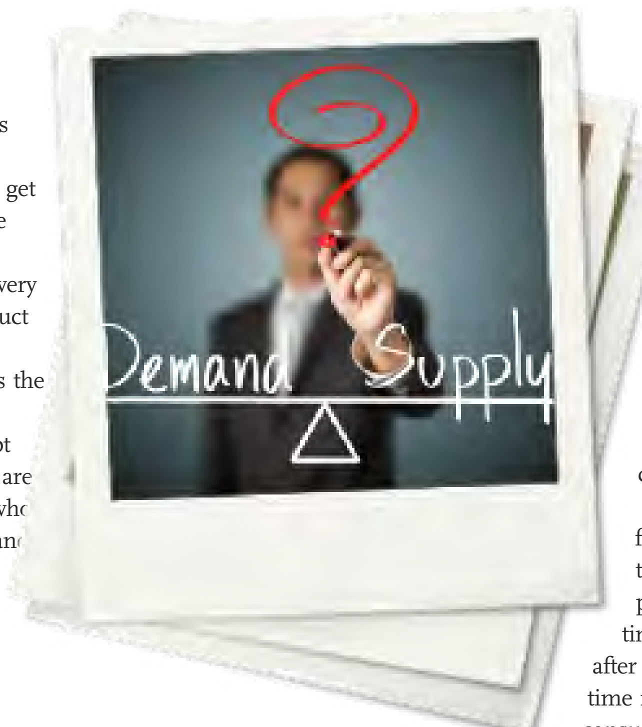
the government has the authority to check the means by which production is done and plan the further process of down streaming as well as income distribution. In simple terms, socialism is about availability of all things to each and every human in a particular area, state, or nation. Although the price mechanism has a little role to play in this type of economy, the idea of socialist economy will show positive results in the long run for any country. It majorly supports the idea of collective ownership in which not a single individual has the right to hold private property beyond the limit prescribed by the government. Thus, all the resources will be utilized by keeping the idea of social welfare in mind, and government will propose the necessary laws to carry out these functions properly.

Unlike mixed economy, there is no competition between private and public sector for resources. Also, there is no class struggle in socialist economy because it treats rich and poor with same eyes and takes care of needs and preference of both. There is a systematic economic plan which is same for all the sections of society under similar circumstances. The central planning authority has the responsibility to lay down this plan and all the issues of this economy will be solved centrally as per the plan. There is no division of labor for private and public sector, and the whole process will be carried out in a centralized and organized manner.

- All the decisions about the production of goods and commodities are taken within the framework laid out by central plan.
- The decision about nature, price, and quantity of the good will be taken by the central planning authority based on the priorities of people in that particular society.
- The plant managers are required to fix the average price of producing a given output which is minimum and feasible for common man.
- The manager should select the scale of output which equalizes the marginal cost.

If the price of good is more than the average cost, the production plant will gain profit and it price is below average, the production plant will face loss. In the former case, the industry would expand its unit, but in latter case it will put the production at halt. In either case, the industry is supposed to reach the equilibrium position.

CONCEPTS IN PRICE MECHANISM



IN TODAY'S DAY and age, money is power. It has the power to control almost everything in the world and get almost anything you want. With the increasing levels of income and affordability rate, the demand for every basic commodity to expensive product has been increasing invariably. The price mechanism which determines the supply-demand ratios based on the buyer-seller relationship is a concept that is well known to all. But there are some resources and commodities whose prices don't follow the supply-demand curve and are determined by other external factors or forces. Let us discuss some of them briefly:

Free price system

The free price system refers to an economic system where the prices of every commodity is determined by the reciprocity of the demand and supply, to signal the resource allocation with reference to the fluctuations in the monetary prices. These signals are communicated between the consumer and producer which acts a guide towards the production, distribution and allocation of resources.

With the help of this free price system the supplies are apportioned, resources are allocated and income is split. Unlike the fixed or controlled price system where the prices are fixed by the government in a planned economy or a controlled market, the free price system has no organisation to regulate the prices, in fact it is determined by the relative supply and demand states.

The prices are determined in a decentralised manner wherein the sellers and the buyers negotiate the prices and come to an agreement after which the trade takes place. When there is a surge in pricing for any particular commodity which is high in demand reflects that the stock and supply is limited. The producers or sellers are intimated about the relative values through the price signals. Due to their limited resources, they negotiate the prices accordingly and a common and agreeable market value is then established between the producers and the consumers.

As the consumer's mind is fickle, that reflects on the demand too. So if something is extremely popular for a particular period of time, it might not be much sought after when the dust settles. By this time in order to meet the high levels of consumer demands the commodity is well stocked and now with the decline in demand, the prices of the commodity also need to be dropped to make sure all of it is sold. This way the lowering of prices signal the producers to control the production as the demand for it has dropped by then.

Trigger price mechanism

This mechanism can be best understood with the help of an example. Let us assume that a country might have a law stating that if a product being imported into their country is valued less than say suppose 20$ per unit, a tariff is levied on the product which finally results in its value being raised to 25$ per unit.

Trigger price is the price at which the product being imported into a particular country is automatically imposed with a tariff or excise, this increases the price by some value, and this is known as the trigger price mechanism.

Trigger prices are generally used when the importing country wishes to encourage free trade but does not wish to let the importers overtake the market and kill the domestic industry profits.

This helps the government regulate the prices in the market irrespective to origin of the product, this is why the imported goods usually have higher prices than the domestic goods. It is the government imposed tax that makes it look more expensive.

Planning and price mechanism

With the market suffering with uncertainties and imbalance, it becomes necessary to take necessary measures to lay out a proper plan to make sure the price mechanism works seamlessly. With the growing realization of inequalities of income and property, there has been a widespread agreement about what can be done to curb the uncertainty. In addition to all this the exploitation of the consumer's interests by the supplier and the seller makes maintaining the equilibrium a lot more challenging issue.

In order to make sure that the prices don't plunge or plummet each time there is either an increase or a decrease in demand of the basic commodities.

Administered Price Mechanism

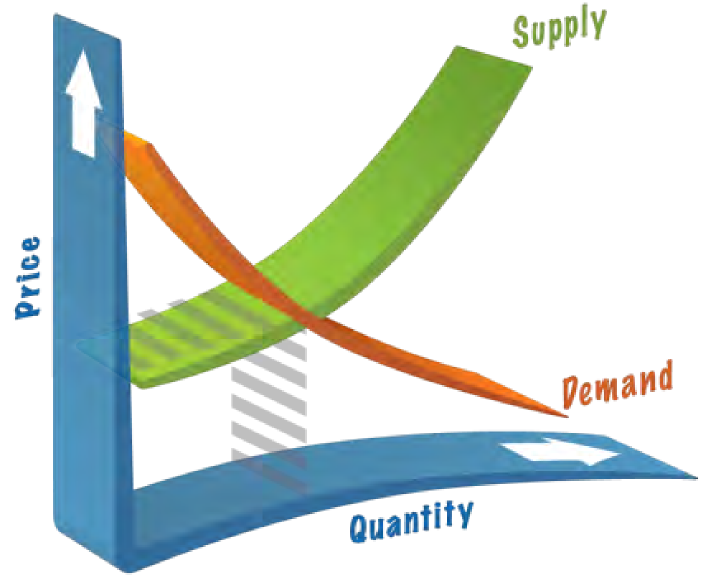
When the price of a good or a commodity is controlled or dictated by the government or an organization, that price is known as the administered price and this mechanism is known as the administered price mechanism.

The regulation of prices is only for certain essential commodities which the government needs to ensure that it is accessible to all.

For example, gas prices are regulated by the government to prevent price gouging during the times of inadequacy. Rent controls are also applied to make sure everything meets a standard of reasonableness.

The price controls can specify an upper limit or price ceiling and a lower limit or price floor (minimum retail price for a particular good or service). This way the costs are stabilized for essential commodities such as sugar, staple foods, goods, bank interest rates and fees according to a rational standard.

In case of a supply and demand change for a particular good, the administered price is bound to change to subsidize



the producer or to protect the buyer.

The abolishment of the administered price mechanism can lead to private industries rapidly setting up retail operations resulting in a sudden rise in prices of that particular commodity. This is how the fuel prices keep rising day by day. Since it is an essential and is in deficit, people are ready to pay any amount at the time of natural calamities. This results in total chaos and the prices skyrocket to meet the demand supply imbalance. In cases like these, it is essential that the government or any governing agency takes control of the situation and makes sure the prices stay in the levels of affordability and reach.

As you can see the price mechanism influences the market in a lot of ways. With the signals from the prices, the consumers and the producers can understand the changes in the market condition with respect to a better understanding of the supply demand situation. If the prices are too high for a product, it is high in demand but is short in supply, this would signal the producers to produce more to meet the demands. If the prices are low, this means the demand is low and supply is higher, this signals the producer to halt the production for a while to avoid overstocking. This is the scenario of a free market system where the negotiations between the producer and the consumer play an active part in deciding the prices

In case of a trigger price mechanism the importers would be levied with an extra duty for importing that good into a foreign country's market making the prices higher than usual this way, the government can make sure the imported goods don't overtake their domestic market.

In case of the administered price mechanism, the government regulates the prices of the essential commodities to make sure they stay in the levels of affordability and reasonableness. This is usually more prevalent in the oil or fuel pricing since they are scarce in nature and are always in demand.

OPINION

WHEN WE LOOK at all the facts, analysis, reports, and graphs based on price mechanism, it is clearly visible that it is one of the burning issues of present decade. After moving ahead of corruption and terror financing, the upcoming matter which should be highlighted is price mechanism. The price mechanism undoubtedly lies at the heart of the market economy. It is the central mechanism which guides the firm and production unit on what to produce, how to produce, and for whom to produce in the market. People invest their hard earned money into the products they want to use and consume. Thus, price mechanism is the deciding factor about what is preferred in the market of goods and commodities. It helps the firms to decide what they are supposed to produce and how much of the capital should be spent for the production. Therefore, the prices of the goods are a clear reflection of the demand for their profitability. These prices are more or less like a signal to the producers that they get from the market or through change in the pricing policies of other organizations. Using these signals along with the tools of price mechanism, the producers get to decide what they must actually produce. After deciding what to produce, the next step of the firm is to make a plan for how to produce. In every domain, there exists a process of natural selection which substantiates the better from the best. The world is all about the survival of the fittest and one has to level up its performance with respect to its competitor, especially in the domain of trade and business. In the market economy, it is quite obvious that each and every firm will try to maximize its profit. And, the ultimate way of doing it is by keeping the prices below the price proposed by its competitor. The organization that fails to do so, will eventually lose its importance in the market and will be eliminated after a certain period of time. In order to ensure its survival in the market and earn maximum profit, the firm must necessarily combine the inputs which are cost effective. In this way, one can undercut the prices of its competitors and increase the market value in a streamlined manner. Amidst all these processes, the price mechanism plays an extremely important role in helping the firm decide about each and every step they must take.

The cost of production has different factors and there are many elements in the production unit which must be taken care of. The prices of these factors also act as signals for the producer to decide what method they should employ for better production techniques. It must be ensured that the factors employed must be cheaper with respect to their marginal revenue of product. Thus, the price mechanism is the key which leads to an efficient allocation of resources in their least combination to the entrepreneur. There are several effects of price mechanism which are important to highlight. It helps in achieving both the technical and economic goals of the organization in an efficient manner. With this, one can make sure that not only there is a minimum wastage of resources but also these resources are utilized to their maximum extent for a more finished product and its genuine use. In other words, price mechanism is not just the backbone but also an invisible hand to guide the young and less experienced entrepreneurs to gain maximum profit and better output from their business. Unlike other rules and regulations of the economy, price mechanism is extremely flexible which provides enough room to change the system and methodologies as per the changing economic circumstances. It makes sure that right product is reaching to the consumer in a satisfactory amount, after all customers is the one which decides the fate of a business by either accepting it or rejecting it. Ultimately it is in the hands of consumer to decide whether they are happy with the product or not. There is one term known as "exclusiveness" which is not discussed in the previous sections. This term is also one of the major deciding factors. Because it aims to protect the spiritual and emotional value of a product which is the right of the consumer. Hence, when an interest becomes exclusive choice of society, it also becomes the right of consumer which should be protected in every manner.

Out of all the types of economies, the free market economy is one which is preferred the most. We know that it is a concept which does not exist in its original form and always faces an intervention from other participants. This free market may come with many uncertainties as people do not have exact information and details about the future of the goods. In order to make this free economy system work efficiently, the producers must be well aware of the goods and commodities. These uncertainties occur when there is no proper distribution of information about a particular good. There are very few people who understand the technical things of a particular good, and hence, they fail to judge a commodity in a proper way. This is one of the major causes of dullness in their business as well as economic activities. There is another factor which is important to know in order to avoid the market failures and risks. This is externality which is, in general terms, a side effect on an individual due to the actions of another individual. When you take decisions or make changes in any of your policies regarding economy which may include production, selling, and buying, your action will have an indirect effect on the people who are not internally related to your business, organization, or market. This is nothing but externality. When we talk of externality, it is of two types i.e. benefit and expense. Let us explain these two aspects using simple example. When a dam, road, or bridge constructed, the benefit goes to all the public who will be using that public service. It is the benefit caused by one individual to other individuals in an indirect manner. Similarly, when a factory is set up in a clean village or town, the fumes cause air pollution. This is the example for expensive externality where one decision of an individual affects a number of people in a negative way. When we seek the opinion of economic enthusiasts, they strongly suggest the idea of conventional production and business which is beneficial for all. One must not look at their own benefit, instead they must also take the safety and security of others into account for going hand in hand with their comfort and requirement. This will lead to flourishing of business because consumers are always attracted towards the healthy business and they prefer to go with the product which not only offers right value of their money but also ensures that it is produced in a user friendly manner. Another way in which one can achieve economic efficiency is through overcoming the monopoly in the market. Usually we have seen that there is always one firm which decides the potential of the market and sets a benchmark for branding, quality, and price. Other firms are supposed to set their standards at par with the organization which is having monopoly in the market. If they fail to do so, their existence in the market remains temporary and soon their product and business vanishes like a fog. This leads to dwindling of efficiency of the economy of a particular country and it should be monitored that each and every firm gets its own space to flourish as per their convenience.

In order to have a balanced market, one must make sure that all their target consumers are getting to know about their product. For example, when we see the public goods or services, we do not see equality in all places. In cities and towns we have light and well constructed roads, but the same is not available in remote areas and villages. Similarly, there are some goods which made with an aim to bring about a change in the society and market but it does not happen because it is not able to reach every consumer in the right way and right form. Many of the consumers remain unaware of number products, whereas others have already used and switched their preferences. In the light of aforesaid facts, the ultimate aim of this section is to create awareness on how to maintain a balanced market by keeping the ideas of price mechanism in mind. It is as simple as the terms demand and supply. We must implement the concept in appropriate manner and meet the economic goals in a right way by keeping all the aspects in mind. One must think rationally and then start a business exploring sufficient examples of success and failures. In this modern era or tools and technology, price mechanism still holds a lot of power to make a business work like never before.

"In order to make this free economy system work efficiently, the producers must be well aware of the goods and commodities. These uncertainties occur when there is no proper distribution of information about a particular good."

Pyush Misra
Director
Consumer Online Foundation

SUPPLY vs DEMAND

PRICES TOTALLY DEPEND on shortage and surplus. It has vice versa effects to it, when there is shortage the prices increase substantially whereas when there is surplus then the prices usually fall.This most of the times happens with the products which are newly introduced or already in and are not very familiar to people. The producers will either get encouraged by the price fluctuation or there would be disappointment, for example- If there is a rise in price of a product then the producer would be more than happy to sell it as it will obviously make them earn more profit. And If the prices falls down they have to look at many ways to sell the product as there would be surplus of the product.

The same goes with the market analysis if the demand for a particular type of labor has increased its production supply, the shortage will go up as the wage rate, and hence reduction of firm's demand of that kind of labor and it has led more workers to do that type of job. It will continue rising until the supply and the demand are balanced or equal. The allocation of all the supply and demandonly depends on the market and no government interference is needed. The market can only run freely if there are no restrictions from the political side.

Government can only intervene when there are issues about capital and land. It depends on the consumer whether to buy the product or not. The same goes with the workers if they don't want to work in a particular industry then no one can force or coerce them. Price mechanism effects are totally dependent on the demand and supply of the market. It is based on assumptions like consumer wants, the value for money given to purchase whereas the suppliers want a profit from the selling of the product. It all depends on the firms which are developing and playing the sellers role, if there are increasing sellers then there are more chances of making the buyers satisfied with good service.

The economy depends on the market and if the market demands for a change then the economy has to do the changes and economy of that particular country depends on the consumers and the products which are sold. National income of the country relies on the demand and supply of the product. The reason unemployment is increasing is because the government is yet to take the important measures to allocate labor to the industry according to their ability. There is always a gap between distributing the wealth because some of the population already have it and some are working hard to get it. The government is still trying to create a free market so that it can be a huge boost to the economy and helps to develop more industries. The market is flexible and it changes according to the consumer, it's needs and demands towards the product, policies are made by government in accordance with the changing society.

AFTER READING EVERYTHING in detail about the concept of price mechanism, here are some of the important points which are worth the spotlight. This will prove to be useful for brief reference to the readers and will create awareness amongst them.

- The system of controlled price mechanism prevails in countries which are either socialist of communist. In this system, the government of the respective country holds an exclusive right to check the production, distribution, and consumption process. The central authority of any country has the responsibility to solve the basic matters related to the matters such as what to produce, how to produce, and for whom to produce.
- The authority has taken steps to enable the proper distribution of various goods at genuine price through ration shops or fair price shops. This is in order to reach out to the consumers in a friendly manner and set a healthy culture of price mechanism.
- Price ceiling is a method which is imposed by government and implemented by the central planning authority. In this system, the government limits the pricing of goods and products which are supplied to them.
- Price floor is also a system of that determines how much price value goes for a particular commodity and it is imposed by the government of the respective country. It has a crucial role to play in agricultural development because it makes sure that both buyers and sellers are receiving genuine price for the commodities.
- In public distribution systems the food grains are distributed at subsidized rates to the poor people and all the process is maintained by coordination of both state and central government.
- Rationing function of price, in simple words, is uplifting the price of the goods when demand gets high and resources are scarce. In short, the greater

the scarcity of the goods, the higher will be the price and higher will be the rationing of the resource.

- Price mechanism, in simple terms, is a system of deciding the price for goods and commodities based on the forces of demand and supply. The buyers and sellers are the major deciding factors that bring about a change in the pricing of goods and commodities.
- In signaling function, the market price adjusts according to the increase or decrease in the demand and supply of the resource.
- Transmission of preference is all about conveying the change in needs and demands to suppliers so that they can also alter their supplies to the market.
- Controlled use of money would combine as much as possible of the decentralized freedoms and peculiar efficiencies of the price mechanism with that extra extension of the field for State planning and control over total money demand, over the distribution of income and property, and over private monopoly which is necessary to avoid the chief evils of the interwar system.
- Higher prices provided as an incentive to the producers to supply goods more because they provide the possibility of more revenue increases and so does the profits. The incentive functions when there is a rise in price, it is associated with an extension of supply along the existing supply curve of the production.
- In the market of shoes, there is a group of people who have money and want shoes (demand). On the other hand, there is a group of people who have shoes and they want money (suppliers). The aim is to produce the right amount of products in the right place and maintain the equilibrium of demand and supply.
- When looked at the concept graphically, it clearly indicates that supply curve (SS) and demand curve (DD) indicates the quantities supplied and demanded and it strictly relies upon price of the commodity. These two curves are helpful in determining how the prices and quantities are fixed in the market.
- The price determination is not an easy process and it involves good number of steps such as market segmentation, estimate demand, marketing mix, pricing policies, pricing strategies, and pricing structure. The prices are determined in the light of marketing opportunities, competition, and many other valuables which are influencing the pricing factors.
- An inefficient market is an economy where social optimality is not achieved and the resources are not optimally allocated. The governments intervene in the markets to address this inefficiency.
- The black market is the venue where all the transactions and businesses take place outside the government authorized channels. These dealings usually occur under the table and this allows them to skip the government levied taxes and price controls. It is completely illegal and is considered as a federal or criminal offence based on the product that is being bought or exchanged.
- A subsidy is a benefit given by the government to groups or individuals, generally in monetary form as a cash payment or a tax reduction. It is typically given to relieve the individual from some kind of burden and is often considered to be in the overall interest of the public or a public welfare act.
- Mixed economy is an economic system which includes both socialism and capitalism. It is a system where private property and asset is protected and the private sector is given some amount of economic freedom to use the capital as per their wish.
- Free market economy is a type of economy where there is hardly any intervention from the side of government. In some cases the government poses few restrictions to keep the things going in a streamlined manner, but in most of the cases there is no interference from government.
- A socialist economy is the one where government controls and regulates the economic system to make sure that equal social opportunity is given to the people of respective nation. In socialist economy the government has the authority to check the means by which production is done and plan the further process of down streaming as well as income distribution.
- Trigger price is the price at which the product being imported into a particular country is automatically imposed with a tariff or excise, this increases the price by some value, and this is known as the trigger price mechanism.
- Pollution Pricing Reform (PPR) is the process of the adjustment of market rates to incorporate the direct environmental impact on measurable parameters such as dust and gas exhaust from combustion engines etc. This approach is not the same as the general ecologic taxation schemes, where the measurability of the impact is unavailable on short term or direct comparison of the tax affected choice for investment or operation.

POOJA KHAITAN

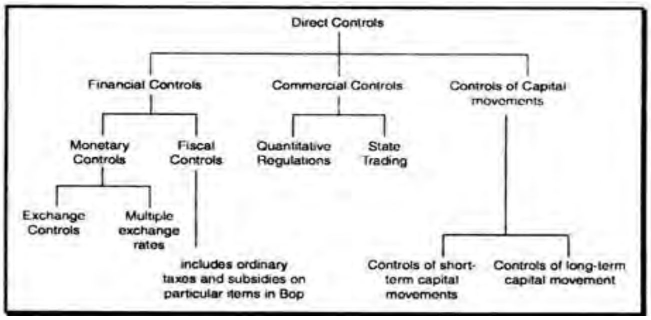
Public distribution systems and rationing: the food grains are distributed at subsidized rates to the poor people and the process is maintained by coordination of both state and central government.

Features and Role:

Controlled Price Mechanism

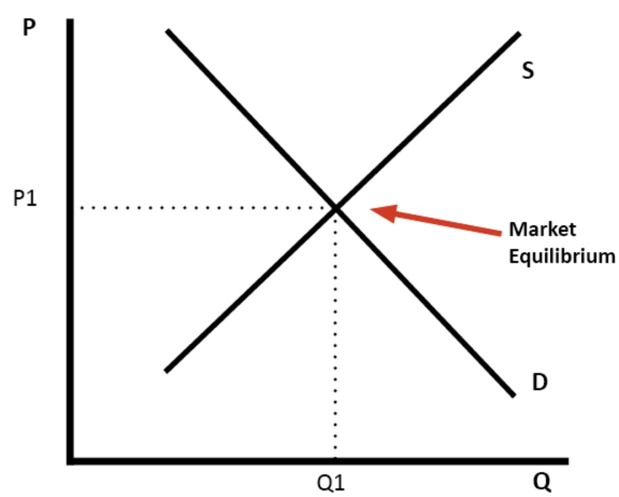
THE CONCEPT BEHIND price mechanism in the economy of any country is to strike a balance in production as well as consumption. All these things include a close inspection of quality and quantity of the products or items which are being produced. As we have already seen that there is no intervening authority between the producers, sellers, and buyers but it is important for someone to monitor each and everything related to this domain. At this point, controlled price mechanism plays an important role in the economy of any country. The system of controlled price mechanism prevails in countries which are either socialist or communist. In this system, the government of the respective country holds an exclusive right to check the production, distribution and consumption process. The central authority of any country has the responsibility to solve the basic matters related to the matters such as what to produce, how to produce and for whom to produce.

The central government has the authority to decide upon the various commodities which the economy is supposed to produce with all the resources which are available for them. The authority ensures that all the goods and services are reaching customers with nominal price and they make proper arrangements for ensuring this. The government can interfere to implement this controlled price mechanism in both direct as well as indirect ways. Before going deep into the matters of price mechanism, we must have a brief look on features and role of controlled price mechanism. In this way, it will be easy to understand how care is taken to give the best to consumers.



Main features of controlled price mechanism are given below:

- The prices are decided and fixed as it is prescribed by the government.

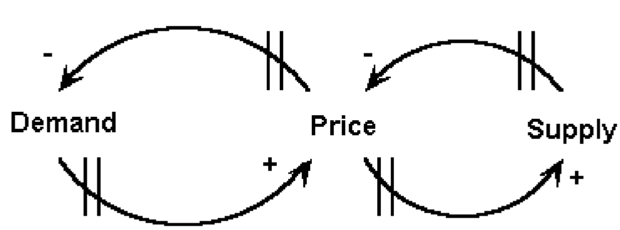


- As already mentioned above, there exists a central planning authority which takes all the decisions related to production as per the rules and regulations laid by the government.
- It is the responsibility of this central planning authority to determine the level of new investment by taking into account the long-term financial goals of the respective organization. The factors such as amount of income, economy, risk tolerance, future needs and expected returns are considered while deciding the level of investment.
- The planning authority is the stakeholder for allocating the resources to make sure that available assets are optimally utilized at right places. A well-structured plan is implemented to support the strategic goals of the respective organization and balance the growing needs as well as priorities to maximize the return on investment.
- The authority has taken steps to enable the proper distribution of various goods at genuine prices through ration shops or fair price shops. This is in order to reach out to the consumers in a friendly manner and set a healthy culture of price mechanism. In this process, it is made sure that consumers receive all the necessary goods at a nominal price and the entire system is coordinated with the help of both central as well as state government. The central planning authority is responsible for procurement, storage, and distribution of the goods into the established network of fair price shops located in different places across the state.
- The government is supposed to take care of all the factors which are related to human resource of the country. The wage rate and interest rate is important for the workers which are a part of production and distribution firms. It is mandatory to keep in mind the needs and expectations of the workers which are supporting the firm manually. By taking care of wage rates and interest rates, the planning authority ensures that there is no exploitation of the man-power available to the firm.

Role of controlled price mechanism

As we have already highlighted that price mechanism can be controlled by the government in both direct as well as indirect ways. Given below are some important roles of controlled price mechanism that will clarify the concept of price mechanism which is controlled by the government.

- **Price ceiling:** This is a method which is imposed by government and implemented by the central planning authority. In this system, the government limits the pricing of goods and products which are supplied to them. This will make sure that consumers are not charged excessively for any commodity they buy.
- **Price floor and agricultural development:** Price floor is also a system of that determines how much price value goes for a particular commodity and it is imposed by the government of the respective country. It has a crucial role to play in agricultural development because it makes sure that both buyers and sellers are receiving genuine price for the commodities. It is important because the prices are made affordable for both middle class and lower class people deprived of quality resources. It makes sure that equilibrium is maintained by decreasing the price for buyers and increasing the gain for sellers.
- **Public distribution systems and rationing:** This is one of the best steps taken to ensure food security for the population belonging to lower middle class and underprivileged section. The food grains are distributed at subsidized rates to the poor people and the process is maintained by coordination of both state and central government. One of the prominent parts of rationing system is fair price shops which are installed in order to ensure that bulk allocation of food grains to different places is properly distributed amongst the needy.
- **Monetary Policy:** The government can make new policies or amend the old ones during the time of inflation or recession. This process is also done by coordinating with central bank of the respective country.
- **Government Expenditures:** We all are aware that expenditure of central government majorly affects the economy of the country. The government has the authority to make changes in tax policy, trade policy, income redistribution policy, expenditure policy, public debts, etc. All these things are done by keeping in mind the needs and expectations of both sellers and consumers.



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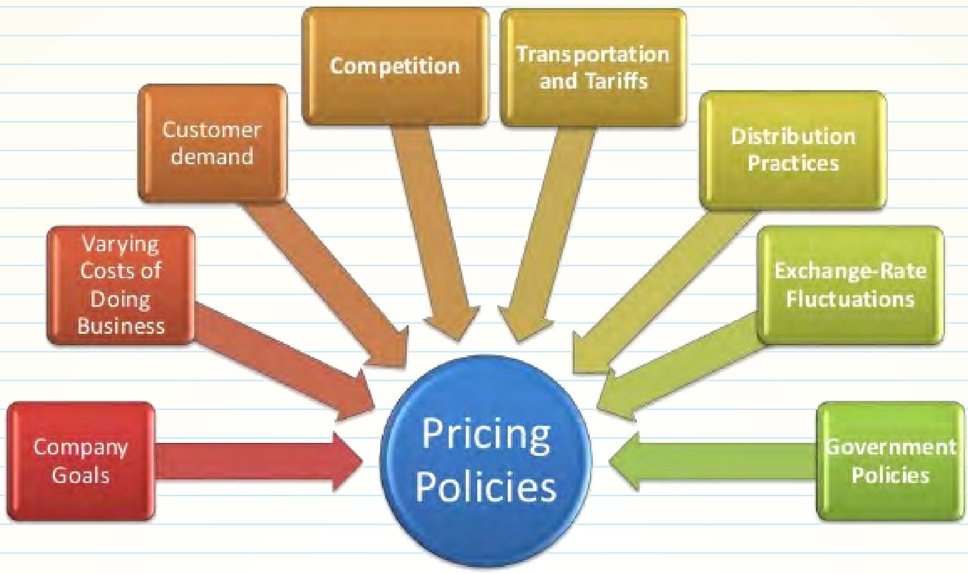

THE PRICE IS determined according to the policies and programmes which are pursued for the development of a nation. When we talk about nation, it does not only include the economy and the money flow. Public's interests are also being taken care of and their protection is also ensured.

In a country like India, where mixed economy prevails, there should be a certain authority that would check the prices in the competitive market. This will keep a check on the price mechanism and on studying the result, consumer protection plans are made. In this way, monopolies can also be kept in control.

Price control also lets the government distribute resources equally among people. This system makes sure that each and every person is able to buy the goods. Otherwise, if price control wasn't initiated, then the rich would have enjoyed all the luxuries and the poor would have no chance to grow.

In a mixed economy, the price control is done looking at the purchasing power and the production goods. This means that demand and supply act as two factors in determining price in a competitive economy. Price control is also needed at times when the product is in short supply.

At times, price control can even become restraint to the demand. When there is a scarcity of certain goods, the prices tend to rise. But even if the demands don't decrease, the prices raise more which creates a blockage for consumers to buy that product.

Prices should be controlled in the market keeping in mind that the market equilibrium is not disturbed. The general price mechanism is, when the supply is low, prices are high and when the supply is high, prices are usually low. This equilibrium is set by the supply and demand.

When a government controls price in a mixed economy, they either set the price of a product higher than the equilibrium market price or lower. This causes instability in the market. The supply of a product might be high, but the government has increased the prices. This situation exploits the consumers' rights as they are unable to buy that necessity, which they might have bought in an equilibrium market.

Similarly, when the prices of a product are set low by the government, then people might keep on buying it more. Here, the pressure of supply falls on the manufacturers as they are slowly going out of stock. At extreme situations, when a necessity product goes out of stock due to low government prices, it creates serious problems in the economy as they are no longer any products to be supplied by the manufacturer.

Price control is a very sensitive issue in a mixed economy. Certain limitations and extreme supervision are required when prices are to be set by the government. If the plan doesn't go according to the requirements, then there can be chances of the economy being crippled for a long duration of time.

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Printed, published & owned by Bejon Kumar Misra, Printed at M/s. Spectrum Printing Press (P) Ltd., Shed No. 23, Computer Complex, DSIDC Scheme I, Okhla Phase II, New Delhi - 110020 and Published at E - 45, Ground Floor, Greater Kailash Enclave - I, New Delhi-110048, Editor: Bejon Kumar Misra