# Shoprite holdings ltd decisions economics essay

Economics

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# Firms' losses and profits

## Economics 101 Essay 2

24 April 2013When a new rivalry firm enters a perfect competitive market system it affects all the existing firms since they are price takers their total revenues are reduced. If the firms are in a long run all factors of production are variable they have to decide on how they produce and if they have to increase their plants or exit the market. Else if they are in the short run they can only partially exit the market or increase the amount of labour since all other factors are fixed. Abstract

## Introduction

The aim Shoprite Private Limited is to maximise its profits so they have to continuously make decisions to remain in business and be more competitive.

## Discussion

## Market system

South Africa's food retailers like Shoprite and Pick n Pay are in a perfect competition market which consists of many buyers and sellers. They also sell identical products such as wheat and milk. These type of market has a free entry and exit therefore they need to adjust until their economic profits are equal to zero. Free entry means competitive firms produce at a price where average cost is minimised. According to Mohr," firms aim to maximise profit (the difference between revenue and cost)", (Mohr, 2011: 223). Profit maximisation requires marginal revenue to equal marginal cost and price equals average total cost. In a perfect competition firms can only make normal profits in the long run and abnormal profits in the short run. ShopRite is in the long run which makes their decisions difficulty to reverse and they can only decide whether to increase outlets or the method of producing each level otherwise they are forced to leave the industry. MC ATCPerfectly competitive firm graphPriceP= MR (quantity demanded)Quantity producedThis market is no longer in the long run equilibrium because of Wal-Mart entry into food retail industry their economic profits are no longer equal to zero. From the article a new competitor Wal-Mart Stores Incorporation the world largest retailer emerged by taking control of Massmart Holdings Ltd for R16. 5 billion this will mean that food retail market competition in South Africa is most likely to increase. Since all firms are price takers they have to be competitive enough since they cannot increase their revenues by charging more to their products because buyers know all prices charged by other firms. Walmart entry causes the industry supply to increase and the supply curve shifted to the right then quantity supplied increases as the prices and economic profit of each firm decreases. Their individual market share is threatened by this situation. as below.

## Shoprite Holdings Ltd decisions

Focusing on the biggest retailer by market value they have to make survival plans to ensure that their total revenues, According to Economics Conditions, " By the assumption they are many firms and each firm is small in size ", (Economics Conditions, 2013; 1). Whenever average total cost is more than the minimum long run average cost the firm changes its plant size to lower average costs and increase economic profit. They cannot affect the market price by producing more of their products so they have to expand their stores to ensure a maximum profit. From the article Shoprite is going to add 106 outlets prior to 96 outlets of the previous year and these stores will be an addition to 1246 stores. Which is considered good for profit maximisation since the world biggest retailer is entering their perfect competitive market.

## Production

Shoprite is a price taker and their economic profit equals to total revenue minus total cost . Since total revenues are equal to price multiplied by quantity sold they to increase what they the quantity of what there are selling. . Price should equal to marginal cost for their business to be profitable. All factors of production for Shoprite can change the number of their machinery and increase the number of their outlets, this therefore classifies them in the long run category. They do not have any fixed costs everything has to be decided from their inputs and how big they want our firm to be. From the article, " Shoprite will add 106 outlets in the 12 months ending June 2012, more than the 96 it opened in the prior year",(Township, 2011: 1). So they have planned to add 74 more supermarkets of which they are expected to hire more labour of between 8000 and 9000 workers. This increases the firm’s production as work will be done more effectively. Marginal revenue is constant and marginal cost eventually increases, profit is maximised by producing the output at which marginal revenue MR equals marginal cost, MC. If Marginal revenues are greater than marginal cost their economic profits increases when there increase outlets. The production of the Shoprite is going to increase since their business is expanding and by the additional outlets. According to the law of supply which states that " Other things remaining the same the higher the price of a commodity, the greater is the quantity supplied and vice versa", (What is Economics, 2013: 1). They have to supply more if the quantity demanded increases but because the demand for most food they are selling is perfectly inelastic they cannot determine how much to sell. But the more there are going to supply there is going to be a slight difference of prices with other which is going to attract more customers. This results in more revenue and it is going to maintain their market value and if successful Shoprite may remain the top food retailer.

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Production FunctionAccording to Parkin " Diminishing returns occur at all quantities of capital as the quantity of labour increases", (Parkin et al, 2010: 232). This explain the law of diminishing marginal product of capital for example.

## Labour Outlet1 Outlet2 Outlet3 Outlet4

4 10 13 1510 15 18 203 13 18 22 244 15 20 24 265 16 21 25 276 1 2 3 4The more the outlets the larger is the total product for any given quantity of labour and the marginal product of capital diminishes with more labour. So Shoprite has to employ the right number of workers to avoid inefficiency.

## Cost

More than one variable inputs allows for factor substitution and to achieve the least cost for each level of output factors will be combined so that the marginal product per unit price of each and every factor is equal. As Shoprite is going to add more firms it is going to incur more production costs because they will now have to pay for more labour and other expenses like electricity bills " The behaviour of long run depends on the firms production function", (Parkin et al, 2010: 232).

## Conclusion

Shoprite has to increase its output by building more of its outlet to avoid economic losses since a new world largest competitor has entered the South Africa’s food retail industry. This decision has to be made because economic losses may force them to leave the industry.