MID-1

ASSIGNMENT-1

1. Define Managerial Economics. Briefly explain importance of Managerial Economics.

Managerial Economics:

According to Spencer & Siegelman, managerial economics as "The integration of economic theory with business practice for the purpose of facilitating decision making & forward planning by management".

Importance of Managerial Economics:

* It gives guidance for identification of key variables in decision-making process.
* It helps the business executives to understand the various intricacies of business & managerial problems & to take right decisions at right time.
* It helps the business executives to become much more responsive, realistic & component to face the dynamic challenges in the modern business world.
* It helps in the optimum use of scarce resources of a firm to maximize its profits.
* It also helps in achieving other objectives a firm likes attaining industry leadership, market share expansion, social responsibilities, etc.

* It provides the necessary conceptual, technical skills, toolbox of analysis & techniques of thinking & other such modern tools & instruments like elasticity of demand & supply, cost & revenue, income & expenditure, profit & volume of production, etc to solve various business problems

* It helps a firm in forecasting the most important economic variables like demand, supply, cost, revenue, price etc. & formulates sound business policies.

* It also helps in understanding the various external factors & forces which affect the decision-making of a firm. Thus, it has become a highly useful & practical discipline in recent years to analyze & find solutions to problems in a systematic & rational manner.

2. What is elasticity of demand? Discuss about significance of elasticity of demand.

Elasticity of demand:-

Elasticity of demand refers to price elasticity of demand which is often called own price elasticity of demand, though the notion of elasticity of demand also relates to income, cross & substitution elasticities of demand.

Types of Elasticity of demand:

1. Price elasticity
2. Cross elasticity
3. Income elasticity
4. Advertising or Promotional Elasticity

Significance of Elasticity of demand:

1. In price Determination of Factors of Production:

It is of great importance for determining prices of various factors of production. In other words, if the demand of a factor is inelastic, its price will be high & if it is elastic, its price will be low.

2. Price Fixation:

The elasticity of demand is the basis of its price determination. The ratio in which, the demand for a product will fall with the rise in its price & vice versa, can be known with the knowledge of elasticity of demand.

3. Government Policies:

The knowledge of elasticity of demand is also helpful for the government in determining its policies

- Tax policy
- Rising bank deposits
- public utility
- Revalution or devaluation of currencies
- Formulate govt policy.

4. Demand Forecasting:

It is basis of demand forecasting. Long-term production planning & management depend more on the income elasticity because management can know the effect of changing income levels on the demand for his product.

5. Planning the level of Output & Price:

For making production profitable, it is essential that the quantity of goods & services should be produced corresponding to the demand for the product. Since, the changes in demand is due to the change in price, the knowledge of elasticity of demand is necessary for determining the o/p level.

3. Give a brief note on a) Production function.
b) Cobb-Douglas PF.

a) Production Function: The production function expresses a functional relationship between physical inputs & physical outputs of a firm at any particular time period. The o/p is thus a function of i/ps. Mathematically production function can be written as,

$$Q = f(L_1, L_2, C, O, T)$$

Q: Quantity of o/p

L_1: Land

L_2: Labour

C: Capital

O: Organization

T: Technology.

Production function can be fitted the particular firm or industry or for the economy as whole.

Production function will change with an improvement in technology.

Production function can be fitted to a short run or to long run.

It is related to a particular period of time

b) Cobb-Douglas Production function:

Production function of a linear homogenous type is invested by Juntwicksell & first tested by C.W.Cobb. This famous statistical production function is known as Cobb-Douglas PF. Originally, the function is applied on the emperical study of the American manufactoring industry.

Cobb-Douglas PF takes the following mathematical form,

$$P = (bL^{a} C^{1-a})$$

P: output

C: capital

L: Labour

$a, 1-a$: Elasticity of production.

The formula function estimated for the USA by Cobb-Douglas is,

$$P = (1.01 L^{0.75} C^{0.25})$$

The function assumes that output is the function of two factors viz. capital & labour.

It assumes that the logarithm of the total o/p of the economy is a linear function of the logarithms of the labour force & capital stock.

4. Briefly explain about various cost concepts in practice?

Cost Concepts: The several alternative bases of classifying cost & the relevance of each for different kinds of problems are to be studied.

The various relevant concepts of cost are.

1. Opportunity costs & outlay costs:- Outlay costs

also Known as actual costs obsolete costs, are those expends which are actually incurred by the firm. There are payments made for labour, material, travel etc..

Opportunity costs implies the earnings foregone on the next best alternative, has the present option is undertaken.

2. Explicit & Implicit Costs :- Explicit involves cash payments, which are actual business cost that appear in account books.

Implicit costs are costs of the factor units that are owned by the employer himself.

3. Historical & Replacement :- Historical cost is the original cost of an asset. A replacement cost is the price that would have to be paid currently to replace the same asset.

4. Short-run & long-run :- Short-run is a period during which the physical capital of firm remains fixed.

Long-run costs are those which vary with o/p when all inputs are variable including plant & capital equipment.

5. Out-of pocket & books cost :- Out-of Pockets are exp-licit costs, that involve current cash payment. Book costs also called implicit, do not require cur-rent cash payments.

6. Fixed & Variable :- Fixed costs remain constant for a certain level of o/p. It is not affected by the changes in the volume of production. Variable is that, which varies directly with variation in o/p.

7. Past & Future :- Past costs are historical, that incurred & recorded in the book of account. Future costs are costs, that are expected to be incurred in the future.

8. Traceable & Common :- Traceable / direct cost, is one which can be identified with product. Common costs are attributed commonly to a particular process or product.

9. Avoidable & Unavoidable :- Avoidable costs can be reduced if the business activities are curtailed. Unavoidable / sunk costs, there will not be any reduction, even business activity is reduced.

10. Controllable & Uncontrollable :- Controllable can be regulated by the executive who is in charge of it

The costs that are independent of actions of execu-tive are called uncontrollable costs.

11. Incremental & sunk: Incremental / different Cost is additional cost due to change in level or nature of business activity.

Sunk costs are those which are not altered by any change.

12. Total, average & marginal :- Total cost is the total cash payment made for the i/p needed for production.

Average cost is the cost per unit of o/p. (TC/Q)

marginal cost is additional cost incurred to produce additional unit.

13. Accounting & Economics :- Accounting costs are costs recorded for the purpose of prepairing the balance sheet.

Economics concept considers future costs & future revenues, which help future planning, choice.

5. What is Break Even Analysis? Explain advanta-ges & Limitations of BEA.

Break Even Analysis :- The study of cost-volume-

-profit relationship is often referred as BEA.

In it's narrow sense, finding out BEP; It is the point of no profit, no loss.

Advantages:-

1. Information provided by BEA to ascertain the profit on a particular level of sales volume or a given capacity of production.

2. to calculate sales required to earn a particular desired level of profit.

3. To compare the efficiency of diff. firms.

4. To decide to 'make or buy' a given component.

5. To compare product lines, sales area, methods of sale for individual company.

6. To decide what promotion mix will yield optimum sales.

Limitations of BEA:

BEA has certain underlying assumptions which form its limitations.

1. Break-even point is based on fixed cost, variable cost, & total cost. A change in one variable is going to affect the BEP.

2. All costs cannot be classified into fixed & Varia-ble costs.

3. It is based on fixed cost concept & hence holds goods only in the short-run.

4. Where the business conditions are volatile, BEP cannot give stable results.

5. In case of multi-product firm, a single chart cannot be of any use. Series of charts have to be made use of.