02-17

UNIT-I: INTRODUCTION TO MANAGERIAL ECONOMICS

→ Managerial Economics
= Management + Economics

→ First Principle:
minimize the cost
Maximize the profits / returns

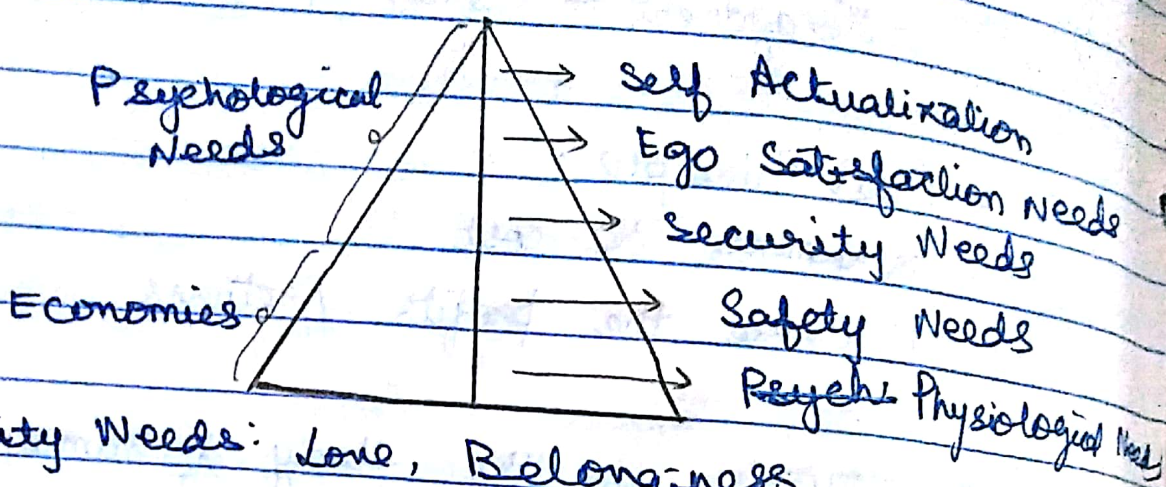
→ Economics is the study of human activity in two levels:
i) Individual level → Micro Economics
ii) National level → Macro Economics

→ Earlier, Economics is regarded as "Science of Wealth"

→ Economic Activities:
Earning and spending money, dates on
Marshall called Economics as Science of Human Wealth, "wellfare" → micro level

→ Economics is a wide subject where nothing is perfectly right or perfectly wrong

→ Theory of Needs:



Security Needs: Love, Belongingness

Maslow developed the theory of needs in 1943

→ Economics is the study of nature and uses of national wealth.

— Adam Smith

→ macro level

→ Economics is the science which studies human behaviour as a relationship between ends and scarce means which have alternative uses.

— Prof. Lionel Robbins

→ Salient features of economics according to Robbins

i) People have unlimited wants

ii) Scarce Resources

iii) Alternative Uses

iv) Choice

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→ According to Keynes, Economics is the study of the administration of scarce needs and determinants of employment and income.

→ How economics is useful to Engineers.

→ Basic Economic Tools:

i) Opportunity Cost Principle
ii) Incremental Principle
iii) Principle of Time Perspective
iv) Discounting Principle
v) Equimarginal Principle

→ Scope of ~~(Managemental)~~ managerial Economics (M.E.)

i) Demand Analysis and Forecasting
ii) Cost ~~and~~ and Production Analysis
iii) Pricing - Decisions, Policies and Practices
iv) Profit Management
v) Capital Management
vi) Competition
vii) Product Policy, Sales Promotion and Market Strategy

i) **Demand Analysis and Forecasting:**

Any business when started, an enterpreneur or a manager needs to find out nature and amount of demand for the product in two time perspectives which are, present demand and future demand and the firm's performance and profitability depends on how the product is forecasted.

NOTE: Four P's in marketing:

Place, Price, Promotion, Product
(Availability) (Quality)

A firm's performance and profitability depends on estimate of demand.

A firm will prepare its production schedule on the basis of demand forecast.

Niche Marketing - Only selected people have the product.

Demand Analysis helps the organizations to identify the factors which create demand for the firm's products and services. It also helps in business planning output levels.

ii) Cost and Production Analysis

* **Cost Analysis:**

Customers expect a good product, i.e., a quality product at a reasonable price which is possible only if manager has control over the cost. The main objective of any business organization is profit maximization which can be achieved by producing the product at a desired level of output at a minimum possible cost.

Cost is the expenditure incurred by the manufacturer in producing the goods/products and services.

Price is what the customer pays for the goods/products and services.

$$\text{Price} - \text{Cost} = \overset{+ve}{\text{Profit}} / \overset{-ve}{\text{Loss}}$$

* **Production Analysis:**

Production Analysis is narrow in scope compared to cost analysis. It is expressed in physical terms whereas the same is expressed in monetary terms in cost analysis.

- Topics under C & P Analysis (UNIT - III)

Cost concepts, cost classification, cost output relationship, production function, cost output

iii) Pricing : Decision, Policies and Practices :

When output is ready, a firm has to fix the price taking the market conditions into consideration. Pricing plays a very important role as a firm's revenue (income) depends on the pricing policy of the organization.

Topics under pricing policy : Price Determination in various markets (perfect market - many buyers & many sellers, monopoly - 1 seller, many buyers, oligopoly - few sellers, many buyers), Pricing Methods (differential pricing, product line pricing, price forecasting)

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Stage	Period	Economist	Focus
Classical	1776	Adam Smith	Wealth
Neo-Classical	1885	Alfred Marshall	Welfare
New	1932	Lionel Robbins	Scarcity / Choice
Modern	1936	J.M. Keynes and Samuelson	Scarcity with reference to employment - income

Evolution Of Managerial Economics

18-12-17

iv) Profit Management:

Profit management is the most difficult area of economics. Objective of every business firm is to gain profit. To maximise the profits, a firm has to take care of : i) Pricing ii) Cost iii) Investment Decisions iv) Capital Budgeting

The topics covered under profit management are
i) Nature of Profit ii) Measurement of Profit
iii) Profit Policies iv) Techniques of Profit Planning
v) Break-Even Analysis vi) Cost-Volume-Profit Analysis

v) Capital Management

Capital Management is very complex in nature. The more investment you make, the more complex it is. Capital management involves: i) Planning ii) Acquisition iii) Disposition and iv) Control of Capital Expenditure

The topics covered under capital management are
i) Cost of Capital ii) Rate of Return and
iii) Selection of Projects

→

vi) Competition:

Competition is an important area of Economics. A manager should have knowledge about the competetors, the different markets and (the conditions in the existing market) external factors.

Topics covered under competition are: i) Perfect Market ii) Imperfect Market iii) Monopoly iv) Oligopoly and v) Price Fixation in different Markets

vi) Product Policy, Sales Promotion and Marketing Strategies

Topics covered under this branch are: i) Product Makes, ii) Sales and Production strategies and iii) Market Strategies

Topics Covered in Next Class:

→ Sales and Economics

i) Opportunity Cost Principle
ii) Incremental Principle
iii) Principle of Time Perspective
iv) Discounting Principle
v) Equimarginal Principle

29-12-18

→ Basic Economic Tools and Concepts

1. Opportunity Cost Principle

Opportunity Cost is cost of sacrificing the alternative decision or opportunity is called opportunity cost.

Eg. A person or 'x' devotes his entire time to his own business. He has sacrified the alternative decision of working in a MNC where he can earn Rs. 1,00,000/- per month. So, the opportunity cost is Rs 1,00,000/- per month. If he is taking the opportunity for 12 months at a stretch, then the opportunity cost is Rs. 12,00,000/- per annum.

4 M's in a Business: i) Men ii) Money iii) Machinery iv) Material

Men – Hourly / Contract / Regular

Money – Bank Loan / Loan from friends / Savings

Machinery – Buy / Lease / Rent

Material – Suppliers A / B / C / D

↳ Adding each factor to get output = input mix

↳ profit depends on it

2. ~~Incremental Principle~~ Four factors of production are men, material, machinery and money. With every factor, opportunity cost is associated.

Men, i.e. labour can be hired on regular/contract/hourly basis.

Money - can take a loan, can use savings, can take a hand loan (no interest)

2. Incremental Principle

The term increment means addition. [When we talk about the incremental principle, there are two terms that come to mind in economics:

i) Marginal Cost (Additional Cost) - incurred/spent

ii) Marginal Revenue (Additional Revenue) - income/get

→ Additional cost incurred in manufacturing extra one unit

→ Additional Revenue earned by selling one extra product/unit]

The two basic concepts related to incremental principle are marginal cost and marginal revenue.

* Marginal Cost - Cost added by producing one extra unit/item of the product.

* Marginal Revenue - Additional revenue which is generated by increasing product sale by one unit.

Incremental Cost and Incremental Revenue.

* Incremental Cost (+ve) - Change (+ve) in total cost resulting from a particular decision.

* Incremental Revenue (+ve) - Change (+ve) in total revenue resulting from a particular decision.

According to the principle of increment, a decision is profitable (if it obeys the following conditions).

SWOT
- Strengths, Weaknesses, Opportunities, Threats
- must consider while doing business

i) When it increases revenue more than the cost
ii) It decreases some cost to a great extent though to some extent it increases others
(Men ↓ Material Machinery ↑ Money)
iii) It increases some revenues more than it decreases others
iv) It reduces cost more than revenues

→ Principle of Time Perspective

According to the principle of time perspective, ~~~~ an entrepreneur, when making a decision, must take into consideration of both short term and long term effect (short run and long run) as the decisions directly impact the revenues as well as the cost.

Revenue - Cost = Profit

Example: In a market, a new product ~~~~ is sold below the cost or on relatively small margins in the beginning with the hope of commanding a good market and profits in the long run. ~~By~~

By taking the time perspective i.e. by following the principle of time perspective, the management or the entrepreneur has to take into account two considerations: →

i) If the management or the enterpreneur commits to too much business at low price, it will not have sufficient financial capacity to run the business in long term.

NOTE: For any product to be sold in the market, four P's must be followed: i) Place ii) Price iii) Product iv) Promotion

ii) In market, once the customers are used to low price they demand similar prices (low prices) from the competetors and also from the producer who has made the product available at a low price.

4) Discounting Principle

A rupee (money) is worth less tomorrow than today. Future must be discounted according to the discording principle (future → money in terms) of future for: i) delay ii) risk of future.

Return on money is always more attractive compared to risk.

5. Equimarginal Principle

Allocation of parts of an available resource among alternative activities, products or organizations.

Example: A ~~fir~~ firm ~~Dess~~ has 100 men of labour at its disposal. The firm is engaged in four activities, say A, B, C and D. If the firm allocates the total labour to activity 'A', it has to do that only at the opportunity cost of others. To attain optimum (maximum benifit) allocation, it should calculate profit generated by each activity. If the activity 'B' ~~pays~~ gains Rs. 45 as profit and activity 'C' ~~pays~~ gains Rs. 10 as profit, more and more labour should be used for activity 'B' and it should be reduced for activity 'c'.

eg.	A	B	C	D
	40	45	10	30