INSTITUTE OF MANAGEMENT TECHNOLOGY
Centre for Distance Learning, Ghaziabad

Lead the Future

www.imtcdl.ac.in

Subject Code: IMT-20

Subject Name : MANAGERIAL ECONOMICS

Notes:

a. *Write answers in your own words as far as possible and refrain from copying from the text books/handouts.*

b. *Answers of Ist Set (Part-A), IInd Set (Part-B), IIIrd Set (Part – C) and Set-IV (Case Study) must be sent together.*

c. *Mail the answer sheets alongwith the copy of assignments for evaluation & return.*

d. *Only hand written assignments shall be accepted.*

A. <u>First Set of Assignments:</u>   5 Questions, each question carries 1 marks.

B. <u>Second Set of Assignments:</u>   5 Questions, each question carries 1 marks.

C. <u>Third Set of Assignments:</u>   5 Questions, each question carries 1 marks. Confine your answers to 150 to 200 Words.

D. <u>Forth Set of Assignments:</u>   Two Case Studies : 5 Marks. Each case study carries 2.5 marks.

Objective:

1. The objective of the paper is to explain the concepts of applied microeconomics.
2. The emphasis shall be on theory of the firm, consumer demand, market system, production analysis, theory of cost, capital budgeting and risk analysis.

Contents

INTRODUCTION TO MANAGERIAL ECONOMICS
The Basic Problems of an Economy, Meaning and Nature of Managerial Economics, How Economics Contributes to Managerial Functions, Major Areas of Economics Applied to Business Decisions, The Scope of Managerial Economics
ECONOMIC PRINCIPLES AND CONCEPTS APPLIED
Marginalism and Incrementalism, The Equi-marginal Principle, Time Perspective in Business Decisions, Opportunity Cost, The Concept of Present Value of Money and Discounting Principle, Concept of Externalities, Concept of Trade-off
THE FUNDAMENTAL LAWS OF MARKET: THE LAWS OF DEMAND AND SUPPLY
The Law of Demand: Price-Demand Relationship, The Demand Function, Types of Demand, The Law of Supply, Equilibrium of Demand and Supply: Determination of Equilibrium Price
ELASTICITY OF DEMAND AND SUPPLY
Price Elasticity of Demand, Determinants of Price Elasticity of Demand, Price Elasticity and Marginal Revenue, Promotional or Advertisement Elasticity of Sales, Cross-elasticity of Demand, Income Elasticity of Demand, Elasticity of Price Expectations, The Uses of Elasticity, Price Elasticity of Supply
THEORY OF CONSUMER DEMAND: CARDINAL UTILITY APPROACH
Cardinal Utility Theory, The Law of Diminishing Marginal Utility, Consumer's Equilibrium, Derivation of Demand Curve, Drawbacks of Cardinal Approach
THEORY OF CONSUMER DEMAND: ORDINAL UTILITY APPROACH
The Meaning and Nature of Indifference Curve, The Diminishing Marginal Rate of Substitution, Properties of Indifference Curves, The Budget Constraint and the Budget Line, Consumer's Equilibrium, Effect of Change in Consumer's Income, Effects of Price Change, Income and Substitution Effects of Price Change on Inferior Goods, Complementarity and Substitutability, The Corner Solution: The Extreme Choice, Derivation of Individual Demand Curve, Comparison of Cardinal and Ordinal Utility Approaches, Critique of Indifference Curve Approach, Samuelson's Revealed Preference Theory

DEMAND FORECASTING
The Need for Demand Forecasting, Methods of Demand Forecasting, Survey Methods, Statistical Methods.
THEORY OF PRODUCTION–I: PRODUCTION WITH ONE VARIABLE INPUT
Meaning of Production, Some Production Related Concepts, Production Function, The Laws of Production
THEORY OF PRODUCTION–II: PRODUCTION WITH TWO VARIABLE INPUTS
Isoquant Curves, Marginal Rate of Technical Substitution, Properties of Isoquant Curves, Isoquant Map and Economic Region, Optimum Combination of Inputs, Other Forms of Isoquants, Elasticity of Substitution, Laws of Returns to Scale: Long Run, Analysis of Production, Empirical Production Functions
THEORY OF PRODUCTION COST
Cost Concepts, Short-run Cost-Output Relations, Long-Run Cost-Output Relations, Economies of Scale: why lac decreases, Diseconomies of Scales;Why LAC Increases, Cost Functions and Cost Curves, Modern Approach to the Theory of Cost, Economies of scope
MARKET STRUCTURE AND OBJECTIVES OF BUSINESS FIRMS
Objectives of Business Firms, Profit Maximization, Alternative Objectives of Business Firms
PRICE AND OUTPUT DETERMINATION UNDER PERFECT COMPETITION
The Market Structure, The Features of Perfect Competition, Equilibrium of the Firm, , Derivation of Supply Curve of the Firm, Derivation of Supply Curve of the Industry, Price and Output Determination Under Perfect Competition, Price and Output Determination in the Long-run, Long-run Supply Curve of a Competitive Industry
PRICE AND OUTPUT DETERMINATION UNDER MONOPOLY
Monopoly: Definition and Sources, Demand and Revenue Curves Under Monopoly, Cost and Supply Curves Under Monopoly, Profit Maximisation under Monopoly, Why Absence of Supply Curve Under Monopoly, Monopoly Vs. Perfect Competition: Comparison of Long-run Price and Output, Price Discrimination by Monopoly, Measures of Monopoly Power
PRICE AND OUTPUT UNDER MONOPOLISTIC COMPETITION
Monopolistic Competition and Its Features, Foundations of the Monopolistic Competition Model, Price and Output Determination Under Monopolistic Competition, Analysis of Selling Cost and Firm's Equilibrium, Critical Appraisal of Chamberlin's Theory of Monopolistic Competition
PRICE AND OUTPUT DETERMINATION UNDER OLIGOPOLY
Oligopoly: Meaning and Characteristics, Duopoly Models, Oligopoly Models, The Game Theory Approach to Oligopoly
ALTERNATIVE THEORIES OF THE FIRM
Baumol's Theory of Sales Revenue Maximization, Marris's Theory of Maximization of Growth Rate, Maximization of Managerial Utility Function: Williamson's Model, The Behavioural Model of Cyert and March, Conventional vs Alternative Theories of Firm
PRICING STRATEGIES AND PRACTICES
Cost-Plus Pricing, Bain's Model of Limit Pricing, Multiple Product Pricing, Pricing in Life Cycle of a Product, Pricing in Relation to Established Products, Transfer Pricing, Competitive Bidding of Price, Peak Load Pricing
CAPITAL BUDGETING AND INVESTMENT UNDER CERTAINTY
Capital Budgeting, Determining the Optimum Level of Capital, Investment Decisions under Certainty, Sources and Cost of Capital
INVESTMENT DECISIONS UNDER RISK AND UNCERTAINTY
Concepts of Risk and Uncerainty, Investment Decisions Under Risk, Investment Decisions Under Uncertainty

Reference:
1. *Dholakia R.H., Oza A.N., Micro Economics for Management Students, OUP, Delhi – 1997*
2. *Koutsoyiannis A, Modern Micro Economics, Mac Millan Press Ltd.*
3. *Gupta G.S., Managerial Economics, Tata McGraw Hills 1998*
4. *Henderson James M. & Quant L.E. Micro Economic Theory, A Mathematical approach, McGraw-Hill International Edition.*

ASSIGNMENTS

FIRST SET OF ASSIGNMENTS   **Assignment-I = 5 Marks**

PART– A

1. Discuss the relationship between economics and management functions. How does the former contribute to the latter?

2. Explain the demand function with the help of examples. Draw appropriate graphs where required.

3. What do you understand by price elasticity of demand? Analyse the relationship between price elasticity and marginal revenue.

4. Discuss the Cardinal Utility Theory. How do the cardinalists derive the demand curve? What are its drawbacks?

5. What do you understand by indifference curves? How are they derived? Describe their properties.

SECOND SET OF ASSIGNMENTS   **Assignment-II = 5 Marks**

PART– B

1. Explain the statistical methods of forecasting demand.

2. Discuss isoquant curves and isoquant maps.

3. Analyse the relationship between output and per unit costs in the short run.

4. What are the chief objectives that business firms seek to achieve that concern an economist?

5. What is meant by monopolistic competition? Explain and critically analyse Chamberlin's theory of monopolistic competition.

THIRD SET OF ASSIGNMENTS   **Assignment-III = 5 Marks**

PART– C

1. What do you understand by duopoly? Explain Cournot's duopoly model.

2. Why is a perfectly competitive firm called a price taker and a monopolist a price maker?

3. Write a note on transfer pricing.

4. Define capital budgeting. Examine how the optimum level of capital is determined.

5. Discuss the methods of making investment decisions under conditions of risk.

FOURTH SET OF ASSIGNMENTS   **Assignment-IV = 2.5 Each Case Study**

CASE STUDY - I

In 1997, over $700 billion purchases were charged on credit cards, and this total is increasing at a rate of over 10 per cent a year. At first glance, the credit card market would seem to be a rather concentrated industry. Visa, MasterCard and American Express are the most familiar names, and over 60 per cent of all charges are made using one of these three cards. But on closer examination, the industry seems to exhibit most characteristics of perfect competition. Consider first the size and distribution of buyers and sellers. Although Visa, Mastercard and American Express are the choices of the majority of consumers, these cards do not originate from just three firms. In fact, there are over six thousand enterprises (primarily banks and credit unions) in the US that offer charge cards to over 90 million credit card holders. One person's Visa card may have been issued by his company's credit union in Los Angeles, while a next door neighbour may have acquired hers from a Miami Bank when she was living in Florida.

Creditcards are a relatively homogenous product. Most Visa cards are similar in appearance, and they can all be used for the same purposes. When the charge is made, the merchant is unlikely to notice who it was that actually issued the card. Entry into and exit from the credit card market is easy as evidenced by the 6000 institutions that currently offer cards. Although a new firm might find it difficult to enter the market, a financially sound bank, even one of modest size, could obtain the right to offer a MasterCard or a Visa card from the present companies with little difficulty. If the bank wanted to leave the field, there would be a ready market to sell its accounts to other credit card suppliers. Thus, it would seem that the credit card industry meets most of the characteristics for a perfectly competitive market.

Questions:

1. What are the characteristics of perfect competition that are exhibited by the credit card industry?
2. Discuss the price and output condition of a perfect competition.
3. Do you think the same competitive state is applicable to the Indian scenario?

CASE STUDY-II

The past fifteen years have seen numerous mergers of banks in every part of the US. Invariably, bank managers point to significant cost reduction (increasing returns to scale) associated with consolidation of computer systems, combining neighbouring branch outlets and reduction of corporate overhead expenses as justification. Many of these mergers involved multibillion dollar banks, which appeared to be inconsistent with existing empirical research on bank costs that showed significant diseconomies of scale for banks with more than $25-50 million in deposits. Unfortunately, these studies used data only for banks with less than $1 billion in deposits. In a more recent study, Sherrill Shaffer and Edmond David used data for large banks (those with $2.5 to $121 billion in deposits) and found increasing returns to scale (i.e., declining per unit costs) up to a bank size of $15 to $37 billion. Clearly, the owners and managers of the merged banks knew more about their actual cost functions than did the earlier economic analysts. The consistent pattern of mergers of banks much larger than $24 to $50 million in deposits was strong evidence that the existing research was incorrect.

Questions:

1. How can mergers in the banking industry result in economies of scale (cost reduction)?
2. Do you think the same factors can lead to economies of scale in the banking sector in India?
3. What are the other factors that can lead to economies of scale in the banking sector?