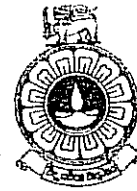


THE OPEN UNIVERSITY OF SRI LANKA  
 BACHELOR OF MANAGEMENT STUDIES PROGRAMME  
 LEVEL 05 – 2005/2006  
 FINAL EXAMINATION 2006  
 MANAGERIAL ECONOMICS – MCU 3207



DATE : 05.03.2006

TIME : 01.30 a.m – 04.30 p.m

**INSTRUCTIONS**

**Duration: Three Hours**

**ANSWER ANY FIVE (05) QUESTIONS.**

**All questions carry equal marks.**

**This question paper has eight questions.**

**Non-programmable calculators are allowed.**

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- (1) (a) How will the knowledge about the co-efficient of price elasticity of demand help a manager in making decisions ? (10 marks)
- (b) How will the price elasticity of supply affect,  
 (i) Garment  
 (ii) Tea industries, in responding to the changing price in the market ? (10 marks)
- (2) (a) Explain (i) Substitution effect  
 (ii) Income effect (05 marks)
- (b) Briefly comment on Income and Substitution effect in relation to Normal, Inferior and Giffen goods. (06 marks)
- (c) Suppose, when the price of good X is Rs. 10/=, 2000 units are demanded and when price increases to 12/= demand drops by 200 units (assume that the demand function is liner)
- (i) Derive the demand function of the good X.
- (ii) If the supply function is given as,  $Q_s = 300 + 50p$  find the equilibrium price and the quantity.
- (iii) What is the price elasticity of demand at price Rs. 10/= ? Comment on the value of the coefficient. (3 marks x 3)

(3) (a) What is break even analysis ? (05 marks)

(b) Prove that the break even output of a firm is given by;  $\frac{TFC}{P - AVC}$

TFC – Total fixed cost, AVC – Average Variable Cost, P-Unit price.  
(05 marks)

(c) Explain the relationship between a firm's fixed cost and the break even level of output.  
(05 marks)

(d) How would the operating leverage technique assist manager in decision making ?  
(05 marks)

(4) Cost structure of a firm is given below.

Output	T.F.C.	T.V.C.	T.C.	A.F.C.	A.V.C.	A.T.C.	M.C.
0	400	0	-	-	-	-	-
1	-	60	-	-	-	-	-
2	-	100	-	-	-	-	-
3	-	130	-	-	-	-	-
4	-	180	-	-	-	-	-
5	-	-	650	-	-	-	-
6	-	-	-	-	-	-	90

(a) Complete the table. (08 marks)

(b) What is Envelop curve ? (04 marks)

(c) Give reasons for the 'U' – shape of long run average cost curve.  
(08 marks)

(5) (a) Explain the market out-come when a perfectly competitive firm is taken over by a monopoly.  
(12 marks)

(b) Suppose demand function of a monopolist is ,  $Q = 100 - 0.5P$ , and the total cost function is,  $TC = 100 + 20Q$ .

(i) Find the profit maximizing output and price. (04 marks)

(ii) Calculate the amount of profit. (04 marks)

- 15) (6) (a) Explain how a loss making perfectly competitive firm determine whether to continue with the production or shut down in the short run. (10 marks)
- (b) "Perfectly competitive markets are extremely rare in the real world" Do you agree ? Explain. (10 marks)
- (7) Write brief notes on the following
- (a) Optimum expansion path.
- (b) Business and Economic profit.
- (c) Cartel.
- (d) Exceptions to Law of demand. (5 marks x 4)
- (8) (a) Briefly explain the relationship among Total Product, Marginal Product and Average Product in the short run. Using the above, explain which stage the rational producer should operate. (08 marks)
- (b) "Short and Long run in the production process vary from industry to industry" Do you agree ? Briefly explain with examples. (06 marks)
- (c) Prove that the firm achieves optimum level of output in the long run, when ;  $\frac{MP_L}{MP_K} = \frac{P_L}{P_K}$  (06 marks)

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