094

**THE OPEN UNIVERISTY OF SRI LANKA**
**BACHELOR OF MANAGEMENT STUDIES PROGRAMME**
**LEVEL 05– 2007**
**FINAL EXAMINATION**
**MANAGERIAL ECONOMICS – MCU 3207**
**DURATION : THREE HOURS**

**DATE : 24.02.2007** **TIME : 1.30 P.M – 4.30 P.M**

***Answer any five (05) Questions. All Questions carry equal marks. Use of non programmable calculators are allowed.***

(1) "A primary role of economics in management is in making optimizing decisions where constrains apply'. Discuss giving examples.

(20 marks)

(2) a) Explain how the following factors determine Price Elasticity of demand.

i. Availability of substitutes
ii. Proportion of income spend on a good
iii. Time period
iv. Nature of the good

( 8 marks)

b) How can the information about price elasticity be useful to managers in business decision making?

(5 marks)

c) Following information of good X, is available.

| Prices (Rs.) | Quantity demanded(units) |
|---|---|
| 8/= | 20,000 |
| 10/= | 19,000 |

Every Rs.2/= change in price, changes the quantity demanded by 1000 units.

i. Find the demand function of good X

(2 marks)

ii. Calculate the Price Elasticity of demand when the price is Rs. 8/=

(2 marks)

iii. Considering elasticity coefficient in question (ii) above, how can the firm increase its revenue, manipulating the price?

(3 marks)

(3) a) i. To produce good X, a firm uses capital and labour. The firm is in a position to change the combination of both factor inputs. Explain how the theory of production help the managers to achieve optimum level of production.

(6 marks)

ii. Suppose price of labour declines, while price of capital remains the same. How will the explanation in part (i) above, change how?

(4 marks)

b) The long run average cost declines due to economics of scale. How will the following aspects help to achieve the economies of scale?

i. Technological factors
ii. Labour factors
iii. Marketing factors
iv. Managerial factors

(10 marks)

(4) a) i. What is Break Even analysis? How will this help the managers in decision making?

(8 marks)

ii. Prove that break even quantity $(Q) = \frac{TFC}{P - AVC}$

(T.F.C – Total Fixed Cost, A.V.C. – Average Variable Cost
P – price)

(4 marks)

b) i. What is Operating Leverage? (4 marks)

ii. Explain how the Operating Leverage helps the managers in effective decision making?

(4 marks)

(5) (a) Explain how the short run profit maximizing output of a monopolist is determined, using

i. Total Cost – Total Revenue approach
ii Marginal Cost – Marginal Revenue approach (6 marks)

(b) What are the conditions that create a monopoly? (6 marks)

(c) The demand equation of a monopolist is given as,

$$P = 400 - 10Q$$

The total cost function is given as,

$$TC = 200 + 10Q^2$$

i. Find the profit maximizing out put and price

ii What is the maximum profit?

P – Price, Q – Quantity

(8 marks)

(6) a) Explain how the oligopolistic firms can use price to avoid active competition. (10 marks)

b) "Efficiency level of oligopoly is higher when the firms in the industry engage in high competition than when they form a cartel" Do you agree? Explain.

(10 marks)

(7) a) "Theoretically Perfectly Competitive Industry is capable of achieving maximum efficiency in the long run, but perfectly competitive industries can not really be found in the real world' Discuss.

(14 marks)

b) The total variable cost is given as.

$$TVC = 120Q - 10Q^2 + Q^3$$

i. Find MC and AVC

ii. Find the output at which AVC is equal to MC.

(6 marks)

(8) Write brief notes on the following

i. Business and Economics profit

ii. Present value of future returns

iii. Marginal Revenue Product of Labour

iii. Income and Substitution effect

(20 marks)