

**THE OPEN UNIVERSITY OF SRI LANKA
BACHELOR OF MANAGEMENT STUDIES – LEVEL 5
ASSIGNMENT TEST – 2011
MANAGERIAL ECONOMICS– MCU 3207
DURATION – TWO (02) HOURS**



DATE : 11th October 2011

TIME : 10.00am – 12.00 noon

**ANSWER PART "A" AND ANY ONE (01) QUESTION FROM PART "B"
NON PROGRAMMABLE CALCULATORS ARE ALLOWED**

PART A

- 1) a) "Rational Decision making requires that all relevant costs, both explicit and implicit, be recognized" Do you agree? Explain with examples. (08 marks)
- b) Estimates of the Income Elasticity of Demand for two food items, given below.

<u>Food</u>	<u>Estimated Income Elasticity</u>
Fish	1.10
Potatoes	0.35

How would fluctuations in consumer income affect the sales as well as the revenue earned from the given two items?

(08 marks)

- c) A particular firm manufactures and sells children's shoes. Management believes that the Price Elasticity of Demand for shoes is (-1.2). Currently shoes are priced at Rs. 600 a pair, and the quantity demanded is 24,000 pairs a year.

- i) If the price is increased to Rs. 720/=, how many pairs of shoes will the firm be able to sell every year?
- ii) How much will total revenue change as a result of price increase?

(09 marks)

- d) Suppose that price of bread increases. How will this affect,

- i) quantity demanded of rice
- ii) quantity demanded of butter
- iii) quantity demanded of computers? Explain using illustrations.

(09 marks)

- ii) Demand for a particular brand of Soft Drink is given as;

$$Q_d = 12800 - 120p$$

$$Q = \text{Quantity} \quad P = \text{price}$$

- a. Compute the Point Price Elasticity of Demand at $P = \text{Rs.}60$
- b. If the objective is to increase the revenue from this product should the price be increased or reduced? Explain.
- c. Compute the Arc Price Elasticity of Demand for price increase from Rs. 60/= to Rs. 72/=

(9 marks)

- iii) What are the constraints faced by a firm in achieving its objectives? Explain with examples.

(7 marks)

(Total – 50 marks)

PART B

- (2) i) “The major goal of any firm is to maximize the present value of future profits. But advocates of alternative theories of the firm argue that behaviour or real world managers is not always consistent with the profit maximization goal” Do you agree? Explain using examples.

(30 marks)

- ii) Using examples explain how Demand Theory and Analysis can be a source of many useful insights for business decision making.

(20 marks)

- (3) a) Explain whether the following statements are ‘True’ or ‘False’. Use illustrations where possible.

- i) Marginal Revenue Product (MRP) is found by multiplying the Marginal Product function by Marginal Revenue.
($MRP = MR \times MP$)

(10 marks)

- ii) Returns to Scale refers to the change in output relative to proportionate changes in inputs.

(12 marks)

- b) The total Cost Function of a particular firm is given as;

$$TC = 120Q - 6Q^2 + 0.2Q^3$$

$$Q = \text{Out put}$$

- i) Is this a short run or long run production function? Provide reasons.
ii) Determine the Average Cost Function and the rate of out put that will minimize average cost.
iii) Determine the Marginal Cost Function and the rate of out put that will minimize marginal cost.
iv) At what rate of out put does average cost equals marginal cost.

(20 marks)

- c) i) How useful is the concept of the Degree of Operating Leverage in business decision making? Explain.

(8 marks)

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