THE OPEN UNIVERSITY OF SRI LANKA
BACHELOR OF MANAGEMENT STUDIES DEGREE PROGRAMME – LEVEL 05
ASSIGNEMNT TEST – 2015 /2016
MANAGERIAL ECONOMICS – MCU 3207
DURATION – TWO (02) HOURS

DATE: 10.10.2015 **TIME: 10.00 AM – 12.00 noon**

INSTRUCTIONS

- Answer any Two (02) questions .
- All questions carry equal marks
- Use of a programmable calculator is allowed.

Question No.01

a) "Managerial Economics combines the economic theory, concepts and known business practices in order to make the process of decision making easy. It is the application of economic analysis to business problems with a view to improving managerial decisions in an organization" Discuss with examples. (25 marks)

b) Compare and Contrast
   i. Profit maximization and sale maximization theories of firm.
   ii. Normal Profit and Abnormal Profit.
   iii. Business Profit and Economic Profit. (18 Marks)

c) "The essence of the science of economics is determining optimum behavior where that behavior is subject to constraints".
What are the constraints on Managerial Decisions?
Explain with examples. (07 Marks)

Question No.02

a) How would the following factors determine the nature of Price Elasticity of Demand of a good? Explain providing examples.
   i. Percentage of income spent on the good.
   ii. Availability of substitutes.
   iii. Nature of the good.
   iv. Time period. (16 Marks)

b) Do you "agree" or "disagree" with the following statements. Explain your answer using illustrations, where possible.
   i. To increase the revenue generated from a good that has elastic demand, the price of the good should be reduced.
   ii. The higher the substitutability of two goods, the higher is the Cross Price Elasticity.
   iii. The value of Income Elasticity of Demand for foreign travel is given as "2.4", therefore "foreign travel" should be considered as a luxury.
   iv. The lower the cost of production the lower is the Price Elasticity of Supply.
   v. When tax is imposed on the supply of a good that has Perfectly Elastic Supply, the entire tax amount has to be borne by the supplier. (20 Marks)

c) The demand function of good 'x' is given as,

$Q_d = 1200 - 16P_x + 0.4I - 12P_y$

Price of $x(P_x)$ = Rs. 20/=, Income (I) = Rs. 10,000/= ,Price of $y(P_y) = Rs. 30/=$.

i. Find the quantity demanded of x at initial prices and income?
ii. Determine what affect a price increase would have on total revenues.
iii. What is the point Income Elasticity of Demand at initial values?
iv. What is the Point Cross Price Elasticity between goods X and Y? Are X and Y substitutes or complements? Explain. (14 Marks)

Question No.03

a) i. Distinguish between Short and Long Run Production.
ii. Would the time encompassing long run production be the same for all the industries? Explain your answer. (12 Marks)

b) Explain whether you "agree" or "disagree" with the following statements. Provide illustrations, where possible.
i. The Law of Diminishing Marginal Returns states that when increasing rates of variable inputs (eg; Labour) are combined with a fixed rate of another input(eg; capital) , the output can be increased continuously.
ii. A firm should hire labour until the value of Marginal Product of labour is equal to the Price of Labour, i.e. Wages (($MRP_L = w$).
iii. Slope of the ISO – quant is equal to the Marginal Products of the two factor inputs. (Consider the factor inputs as labour and capital).
iv. Firm achieves the optimum level of production in the long run at the point where ISO- Quant Curve is tangent to the ISO-Cost Curve. (24 Marks)

c) Explain the following using illustrations.
i. Returns to Scale
ii. Optimum Expansion Path (14 Marks)

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