**Assignment = Managerial economics**

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**Managerial Economics Assignment**

**Question No.1**

Managerial Economics is a discipline which deals with the application of economic theory to business management. Describe the nature and scope of managerial economics in the context of above mentioned statement?

**Answer:-**

**Definition of Managerial Economics:**

“Managerial Economics is economics applied in decision making. It is a special branch of economics bridging the gap between abstract theory and managerial practice.” – Haynes, Mote and Paul.

“Business Economics consists of the use of economic modes of thought to analyse business situations.” - McNair and Merriam

“Business Economics (Managerial Economics) is the integration of economic theory with business practice for the purpose of facilitating decision making and forward planning by management.” - Spencer and Seegelman.

“Managerial economics is concerned with application of economic concepts and economic analysis to the problems of formulating rational managerial decision.” – Mansfield

**Nature of Managerial Economics:**

* The primary function of management executive in a business organisation is decision making and forward planning.
* Decision making and forward planning go hand in hand with each other. Decision making means the process of selecting one action from two or more alternative courses of action. Forward planning means establishing plans for the future to carry out the decision so taken.
* The problem of choice arises because resources at the disposal of a business unit (land, labour, capital, and managerial capacity) are limited and the firm has to make the most profitable use of these resources.
* The decision making function is that of the business executive, he takes the decision which will ensure the most efficient means of attaining a desired objective, say profit maximisation. After taking the decision about the particular output, pricing, capital, raw-materials and power etc., are prepared. Forward planning and decision-making thus go on at the same time.
* A business manager’s task is made difficult by the uncertainty which surrounds business decision-making. Nobody can predict the future course of business conditions. He prepares the best possible plans for the future depending on past experience and future outlook and yet he has to go on revising his plans in the light of new experience to minimise the failure. Managers are thus engaged in a continuous process of decision-making through an uncertain future and the overall problem confronting them is one of adjusting to uncertainty.
* In fulfilling the function of decision-making in an uncertainty framework, economic theory can be, pressed into service with considerable advantage as it deals with a number of concepts and principles which can be used to solve or at least throw some light upon the problems of business management. E.g are profit, demand, cost, pricing, production, competition, business cycles, national income etc. The way economic analysis can be used towards solving business problems, constitutes the subject-matter of Managerial Economics.
* Thus in brief we can say that Managerial Economics is both a science and an art.

**Scope of Managerial Economics:**

The scope of managerial economics is not yet clearly laid out because it is a developing       science. Even then the following fields may be said to generally fall under Managerial Economics:

    1.  Demand Analysis and Forecasting

    2.  Cost and Production Analysis

    3.  Pricing Decisions, Policies and Practices

    4.  Profit Management

    5.  Capital Management

These divisions of business economics constitute its subject matter.

Recently, managerial economists have started making increased use of Operation Research methods like Linear programming, inventory models, Games theory, queuing up theory etc., have also come to be regarded as part of Managerial Economics.

   **1. Demand Analysis and Forecasting:** A business firm is an economic organisation which is engaged in transforming productive resources into goods that are to be sold in the market. A major part of managerial decision making depends on accurate estimates of demand. A forecast of future sales serves as a guide to management for preparing production schedules and employing resources. It will help management to maintain or strengthen its market position and profit base. Demand analysis also identifies a number of other factors influencing the demand for a product. Demand analysis and forecasting occupies a strategic place in Managerial Economics.

  2. Cost and production analysis: A firm’s profitability depends much on its cost of production. A wise manager would prepare cost estimates of a range of output, identify the factors causing are cause variations in cost estimates and choose the cost-minimising output level, taking also into consideration the degree of  uncertainty in production and cost calculations. Production processes are under the charge of engineers but the business manager is supposed to carry out the production function analysis in order to avoid wastages of materials and time. Sound pricing practices depend much on cost control. The main topics discussed under cost and production analysis are: Cost concepts, cost-output relationships, Economics and Diseconomies of scale and cost control.

  **3. Pricing decisions, policies and practices**: Pricing is a very important area of Managerial Economics. In fact, price is the genesis of the revenue of a firm ad as such the success of a business firm largely depends on the correctness of the price decisions taken by it. The important aspects dealt with this area are: Price determination in various market forms, pricing methods, differential pricing, product-line pricing and price forecasting.

    **4. Profit management:** Business firms are generally organized for earning profit and in the long period, it is profit which provides the chief measure of success of a firm. Economics tells us that profits are the reward for uncertainty bearing and risk taking. A successful business manager is one who can form more or less correct estimates of costs and revenues likely to accrue to the firm at different levels of output. The more successful a manager is in reducing uncertainty, the higher are the profits earned by him. In fact, profit-planning and profit measurement constitute the most challenging area of Managerial Economics.

  **5. Capital management:** The problems relating to firm’s capital investments are perhaps the most complex and troublesome. Capital management implies planning and control of capital expenditure because it involves a large sum and moreover the problems in disposing the capital assets off are so complex that they require considerable time and labour. The main topics dealt with under capital management are cost of capital, rate of return and selection of projects.

**Conclusion:** The various aspects outlined above represent the major uncertainties which a business firm has to reckon with, viz., demand uncertainty, cost uncertainty, price uncertainty, profit uncertainty, and capital uncertainty. We can, therefore, conclude that the subject-matter of Managerial Economics consists of applying economic principles and concepts towards adjusting with various uncertainties faced by a business firm.

**Question No.2**

Discuss demand analysis and forecasting under the umbrella of Business Management?

**Answer:-**

**Demand Analysis**

**Definition:** The **Demand Analysis** is a process whereby the management makes decisions with respect to the production, cost allocation, advertising, inventory holding, pricing, etc. Although, how much a firm produces depends on its production capacity but how much it must endeavor to produce depends on the potential demand for its product.

Thus, the marketer is required to analyze properly the demand for its product in the market and must hold inventory accordingly. Such as if there is a potential demand in the future, then the firm should hold more inventories and in case there is no demand, then the production remains unwarranted, and hence, lesser inventories are held.

There is a possibility that production might exceed the demand, and then the marketer must use alternative ways such as better advertisements to create a new demand.

The demand shows the relationship between two economic variables, the price of the product and the quantity of product that a consumer is willing to buy for a given period of time, other things being equal.

## Features/Characteristics of Demand

The following are the main features or characteristics of demand that the marketer must keep in mind while analyzing the demand for its product:

* The demand is the **specific quantity** that a consumer is willing to purchase. Thus, it is expressed in **numbers**.
* The demand must mean the **demand per unit of time**, per month, per week, per day.
* The demand is always**at a price,**e. any change in the price of a commodity will bring about a certain change in its quantity demanded.
* The demand is always in a **market**, a place where a set of buyers and sellers meet. The market needs not to be a geographical area.

Thus, demand plays a crucial role in the success of any business enterprise. And it must be remembered that demand is always at a price and a particular time period in which it is created. Such as demand for woolen clothes will be more in winters than in any other season. Hence, demand analysis is always done in terms of the price and the relevant time period.

# Demand Forecasting

**Definition: Demand Forecasting** refers to the process of predicting the future demand for the firm’s product. In other words, demand forecasting is comprised of a series of steps that involves the anticipation of demand for a product in future under both controllable and non-controllable factors.

The business world is characterized by risk and uncertainty, and most of the business decisions are taken under this scenario. An organization come across several risks, both internal or external to the business operations such as technology, attrition, unrest, employee grievances, recession, inflation, modifications in the government laws, etc.

**Predicting the future demand for a product helps the organization in making decisions in one of the following areas:**

* Planning and scheduling the production and acquiring the inputs accordingly.
* Making the provisions for finances.
* Formulating a pricing strategy.
* Planning advertisement and implementing it.

Demand forecasting **holds significance in the businesses where large-scale production** is involved. Since the large-scale production requires a long gestation period, a good deal of forward planning should be done. Also, the potential future demand should be estimated to avoid the conditions of overproduction and underproduction. Most often, the firms face a question of what would be the future demand for their product as they have to acquire the input (labor and raw material) accordingly.

The objective of demand forecasting is attained only when the forecasting is done systematically and scientifically. Thus, the following **steps in demand forecasting** are followed to facilitate a systematic estimation of future demand for product:

1. Specifying the Objective
2. Determining the Time Perspective
3. Choice of method for Demand Forecasting
4. Collection of Data and Data Adjustment
5. Estimation and Interpretation of Results

Thus, demand forecasting is a systematic process that assumes greater significance in large-scale producing firms. Demand forecasting may not be a serious issue for the small scale firms which supply a small portion of total demand or produces the product that caters to the short demand or seasonal demand. Such firms can plan their production on the basis of the business skills and their past experiences.

**Question No.3**

Business firms are generally organized for earning profits. Explain Profit Management as a challenging issue in the managerial economics?

**Answer:-**

**Profit Management**

Success of a firm depends on its primary measure and that is **profit**. Firms are operated to earn long term **profit** which is generally the reward for risk taking. Appropriate planning and measuring **profit** is the most important and challenging area of **managerial economics**.

"A business firm is an organization designed to make profits and profits are the primary measure of its success." Joel Dean

Business organizations operate within the societies and societies expect quality of products, reliable supply in quantity and place etc. To make profits, firms have to satisfy the desires of the buyers and other stakeholders of the society. The firm can continue as profit system only by satisfying the stakeholders. But within the system of profits, profits are the acid test of the individual's firm's performance.

Joel Dean highlighted three issues regarding profit.

1. Profit measurement - Economic analysis of accounting data for policy making
2. Policy decisions on profit standards and profit goals
3. Use of profits for control purposes in complex business organizations.

Economic Analysis of Profits Measurement by Accoutants

"Economists are unhappy about conventional accounting methods for measuring business income."

Conceptual conflict

Economists look to the future and economic decisions taken today produce profits in the future. For decision making today past is irrelevant, excepting for its use in forecasting for the future.

Joel Dean discussed four issues specially.

1. The types of costs to be deducted from revenues to arrive at profit.
2. Depreciation
3. The treatment of capital gains and losses
4. Price level basis of valuation of assets.

Policy decisions on profit standards and profit goals

Reasons for Limiting Profits

it is an interesting topic and Joel Dean brought into explanation at the start of the topic.

1. To discourage potential competitors.
2. To woo the voting public and restrain the zeal of antitrusters.
3. To restrain wage demands of organized labor.
4. To maintain customer good will
5. To keep control undiluted.
6. To maintain pleasant working cnditions.

Joel Dean highlighted the need for restraining profits and gave some guidelines for determining reasonable profits.
 **Profits for Control**

1. In divisional organization, where products are different:
2. In vertically integrated organization

There is complexity in this issue, and the conclusion is that profit standard for control must be set largely by managerial ukase, designed with discretion and wisdom