

MANAGERIAL ECONOMICS

BBA LLB SEMESTER 1



Question Answer PDF

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MANAGERIAL ECONOMICS

BBA LLB Semester 1 – COMPLETE QUESTION BANK (WITH ALL OPTIONS EXPLAINED)

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◇ A. MULTIPLE CHOICE QUESTIONS (MCQs)

👉 Each option explained to remove confusion

Q1. What is the main purpose of Managerial Economics?

- a) To study the behaviour of individual consumers and firms
- b) **To integrate economic theory with business practice for decision-making** ✓
- c) To forecast macroeconomic indicators like GDP and inflation
- d) To analyze the financial statements of a company

Explanation:

- (a) ✗ This is Microeconomics, not managerial economics
 - (b) ✓ Correct. Managerial economics bridges theory and practical business decisions
 - (c) ✗ This is Macro-economic analysis
 - (d) ✗ This is Accounting/Finance, not managerial economics
-

Q2. Opportunity cost refers to:

- a) The money spent on a decision
- b) **The cost of the next best alternative forgone** ✓
- c) A cost already incurred
- d) The cost of owned resources

Explanation:

- (a) ✗ That is explicit cost
 - (b) ✓ Correct definition of opportunity cost
 - (c) ✗ That is sunk cost
 - (d) ✗ That refers to implicit cost
-

Q3. If price elasticity of demand is 0.5, demand is:

- a) Unitary elastic
- b) Perfectly elastic
- c) Elastic
- d) **Inelastic** ✓

Explanation:

- $PED < 1 \rightarrow$ Inelastic demand
 - (d) is correct
-

Q4. In which market structure is the firm a price taker?

- a) Monopoly
- b) Oligopoly
- c) Monopolistic competition
- d) **Perfect competition** ✓

Explanation:

- (a) ✗ Monopoly sets price
- (b) ✗ Firms influence prices
- (c) ✗ Some price control exists
- (d) ✓ Firms accept market price

Q5. MC intersects AVC at:

- a) Maximum point
- b) **Minimum point** ✓
- c) Point of inflection
- d) Zero point

Explanation:

- MC always cuts AVC at its **lowest point**

Q6. Which is a quantitative method of demand forecasting?

- a) Consumer survey
- b) Delphi method
- c) **Regression analysis** ✓
- d) Sales force opinion

Explanation:

- (a), (b), (d) ✗ Qualitative methods
- (c) ✓ Statistical/quantitative method

Q7. Economic profit equals:

- a) TR – Explicit costs
- b) TR – Implicit costs
- c) **TR – (Explicit + Implicit costs)** ✓
- d) Accounting profit – Explicit costs

Explanation:

- Economic profit includes **opportunity cost**, hence both costs

Q8. Isoquant curve shows:

- a) Same cost combinations
 - b) Same output combinations of outputs
 - c) **Same output combinations of inputs** ✓
 - d) Profit-maximizing combinations
-

Q9. Kinked demand curve explains:

- a) Price flexibility
- b) **Price rigidity** ✓
- c) Product differentiation
- d) Non-price competition

Q10. Sunk costs are:

- a) Opportunity costs
- b) Variable costs
- c) **Irrecoverable past costs** ✓
- d) Fixed costs

◆ **B. SHORT ANSWER QUESTIONS**

(7 Marks Each – Paragraph Form)

1. Price Elasticity of Demand and Pricing Decisions

Price Elasticity of Demand refers to the degree of responsiveness of quantity demanded of a commodity to a change in its price. It is measured as the ratio of the percentage change in quantity demanded to the percentage change in price. This concept is extremely useful for business managers while making pricing decisions. If the demand for a product is inelastic, a rise in price will not significantly reduce quantity demanded and may increase total revenue. On the other hand, if demand is elastic, a reduction in price can lead to higher sales volume and revenue. Thus, knowledge of elasticity helps managers in fixing prices, forecasting revenue, and formulating sales strategies.

2. Accounting Profit and Economic Profit

Accounting profit is the difference between total revenue and explicit costs such as wages, rent, raw materials, and interest paid. Economic profit, however, is calculated by deducting both explicit and implicit costs from total revenue. Implicit costs include the opportunity cost of the owner's own resources, such as self-owned capital or managerial time. From a managerial perspective, economic profit is more relevant because it shows the real profitability of a business after considering all costs. It helps managers decide whether resources are being used in the most efficient manner.

3. Steps in Demand Forecasting

Demand forecasting is a systematic process of estimating future demand for a product. The first step involves clearly defining the objectives of forecasting. The next step is identifying the factors affecting demand such as price, income, consumer preferences, and competition. After this, an appropriate forecasting method is selected and relevant data is collected. The data is then analyzed to estimate future demand. Finally, the forecast is evaluated and revised periodically to ensure accuracy. Proper demand forecasting helps firms in production planning and inventory control.

4. Law of Variable Proportions

The Law of Variable Proportions states that when additional units of a variable factor are combined with fixed factors, total output initially increases at an increasing rate, then at a decreasing rate, and

finally declines. This law operates in the short run when at least one factor of production remains fixed. The three stages of production occur due to better utilization of fixed factors in the initial stage, overcrowding of factors in the second stage, and excessive use of variable factors in the third stage. This law helps firms determine the optimal level of output.

5. Break-Even Analysis

Break-even analysis is a technique used to determine the level of output at which total cost equals total revenue, resulting in neither profit nor loss. Given fixed costs of ₹50,000, selling price of ₹20 per unit, and variable cost of ₹12 per unit, the contribution per unit is ₹8. The break-even point in units is calculated by dividing fixed costs by contribution per unit, which comes to 6,250 units. The break-even sales value is ₹1,25,000. This analysis helps managers assess risk and profitability.

6. Role of a Managerial Economist

A managerial economist plays a crucial role in assisting management with economic decision-making. Their responsibilities include demand forecasting, cost analysis, pricing strategies, profit planning, and capital budgeting decisions. They also analyze market conditions, business cycles, and government policies to guide strategic planning. By applying economic tools and theories, managerial economists help organizations achieve efficiency and long-term growth.

7. Short-Run Cost Concepts

In the short run, a firm incurs different types of costs. Total Fixed Cost (TFC) remains constant regardless of output, such as rent and salaries. Total Variable Cost (TVC) varies directly with the level of output, such as raw materials and wages. Marginal Cost (MC) is the additional cost incurred in producing one extra unit of output. Understanding these costs helps firms in output and pricing decisions.

8. Pricing Strategies: Skimming and Penetration Pricing

Price skimming is a strategy where a high price is charged initially to recover development costs quickly, usually applied to innovative or technologically advanced products. Penetration pricing involves setting a low initial price to attract a large number of customers and gain market share. Skimming is suitable when demand is inelastic, while penetration pricing is effective in highly competitive markets.

◆ C. LONG ANSWER QUESTIONS

(15 Marks Each – Detailed Paragraph Form)

1. Nature and Scope of Managerial Economics

Managerial Economics is a branch of economics that applies economic principles and methodologies to business decision-making. Its nature is prescriptive, as it suggests solutions to business problems. It is multidisciplinary, drawing concepts from economics, statistics, accounting, and management. The scope of managerial economics includes demand analysis, production and cost analysis, pricing decisions, profit management, and capital budgeting. By integrating theory with practice, managerial economics assists managers in achieving efficient resource allocation and business growth.

2. Price Elasticity of Demand: Concept and Importance

Price Elasticity of Demand measures the responsiveness of quantity demanded to changes in price. It is influenced by factors such as availability of substitutes, nature of the commodity, income level, and time period. For managers, elasticity is a powerful tool for pricing decisions, revenue forecasting, and output planning. Understanding elasticity enables firms to maximize profits and respond effectively to market changes.

3. Perfect Competition and Firm Equilibrium

Perfect competition is a market structure characterized by a large number of buyers and sellers, homogeneous products, free entry and exit, and perfect knowledge. In such a market, firms are price takers. A firm achieves equilibrium in the short run where marginal cost equals marginal revenue. At this point, the firm maximizes profit or minimizes loss. This analysis helps understand pricing and output determination under competitive conditions.

4. Production Function and Returns to Scale

A production function shows the relationship between inputs and output. Returns to scale refer to changes in output when all inputs are increased proportionately. Increasing returns occur due to economies of scale, constant returns when output increases proportionately, and decreasing returns due to diseconomies of scale. Understanding returns to scale helps firms plan expansion and production efficiency.

5. Oligopoly and Kinked Demand Curve

Oligopoly is a market structure dominated by a few large firms. The kinked demand curve model explains price rigidity in oligopolistic markets. According to this model, firms fear price wars if prices are reduced and loss of customers if prices are increased. As a result, prices tend to remain stable. This model highlights interdependence among firms.

6. Capital Budgeting

Capital budgeting involves evaluating long-term investment decisions. It is important for growth and profitability. The process includes identifying projects, evaluating proposals, selecting investments, and reviewing outcomes. The Net Present Value method focuses on absolute returns, while the Internal Rate of Return focuses on percentage returns. NPV is considered more reliable for decision-making.

7. Cost Curves and Their Relationship

Cost refers to the expenditure incurred in producing goods. In the short run, Average Variable Cost and Average Total Cost are U-shaped due to the law of variable proportions. Marginal Cost intersects both AVC and ATC at their minimum points. This relationship helps firms decide optimal output levels.