

MANAGERIAL ECONOMICS

Meaning

Managerial economics is a stream of management studies that emphasizes primarily on solving business problems and decision-making by applying the theories and principles microeconomics and macroeconomics. It is a specialized stream dealing with an organization's internal issues using various economic tools. Economics is an indispensable part of any business. This single concept derives all the business assumptions, forecasting, and investments.

Nature of Managerial Economics

1. Art and Science

Management theory requires a lot of critical and logical thinking and analytical skills to make decisions or solve problems. Many economists also find it a source of research, saying it includes applying different economic concepts, techniques, and methods to solve business problems.

2. Microeconomics

Managers typically deal with the problems relevant to a single entity rather than the economy as a whole. It is, therefore, considered an integral part of microeconomics.

3. Uses of Macro Economics

A corporation works in an external world, i.e., serving the consumer, an important part of the economy. For this purpose, managers must evaluate the various macroeconomic factors, such as market dynamics, economic changes, government policies, etc., and their effect on the company.

4. Multidisciplinary

Managerial economics uses many tools and principles that belong to different disciplines, such as accounting, finance, statistics, mathematics, production, operational research, human resources, marketing, etc.

5. Prescriptive or Normative Discipline

By introducing corrective steps managerial economics aims at achieving the objective and solves specific issues or problems.

6. Management Oriented

This serves as an instrument in managers' hands to deal effectively with business-related problems and uncertainties. This also allows for setting priorities, formulating policies, and making successful decisions.

7. Pragmatic

The solution to day-to-day business challenges is realistic and rational. Different individuals take different views of the principles of managerial economics. Others may concentrate more on customer service and prioritize efficient production.

Objectives of Managerial Economics

Make a profit:

Making a profit is the core objective when running a company. A business must make a profit that produces a reasonable return on shareholders' equity investment and provides funds for growth.

Grow and develop the business:

Businesses cannot remain stagnant; they must grow to provide funds for expansion and offer more benefits for employees.

Maintain a regular supply of goods and services:

Managers coordinate sales forecasts with orders for materials, setting manpower levels and scheduling production.

Plan for long-term survival:

Plan for the future. Firms rise above the rest because they can sell more products, manage production more efficiently and control expenses better than their competitors.

Optimize the use of resources:

Managerial economics looks for the best use of resources. This includes labor, capital, cash and fixed assets.

Improve labor utilization:

Workers are most productive when they feel they are being adequately compensated, improving their skills in jobs and have a secure future for employment. The goal is to create an atmosphere where workers want to contribute their best performance to the benefit of the organization.

Minimize risks:

Evaluate market factors using economic analysis for better forecasting and more accurate assessments of risks.

Importance of Managerial Economic

- Tools and Techniques for Better Decision Making
- Solutions to the basic problems of business management
- Formulating business policies
- Cost Control

- Price Determination
- Data for analysis and forecasting
- Business Planning
- Profit Planning and Control
- Inventory Management
- Act as a guide to Managerial economist

Principles of Managerial Economics

- Incremental Principle
- Equal Marginalism Principle
- Marginalism Principle
- Time Perspective Principle
- Discounting Principle
- Opportunity Cost Principle

Types of Managerial Economics

- Micro Economics
- Macro Economics

Microeconomics

This approach focuses on the economic behavior of individual firms, households, and consumers, and how they interact in various markets.

It examines how firms make decisions about pricing, production, and resource allocation to maximize their profits, and how consumers make decisions about buying goods and services based on their preferences and budgets.

Macroeconomics

This approach focuses on the economy as a whole, and how aggregate variables such as GDP, inflation, and unemployment affect the performance of individual firms.

Relationship of Managerial Economics with Other Disciplines or Subjects

1. Managerial Economics and Statistics

Statistical tools are playing very important role in business decision-making. Statistical techniques are used in collecting, processing and analyzing data, testing the validity of the economic laws with the real economic phenomenon before they are applied to business analysis. Probable economic events are the basis of a good business decision. Various statistical tools Such as theory of probability, forecasting techniques etc., help the decision-makers in the prediction of future economic events.

2. Managerial Economics and Mathematics

The main challenge of a businessman is how to minimize cost or how to maximize profit or how to optimize sales. To find the answers of these questions, various mathematical concepts and techniques are widely used in economic logic. The knowledge of geometry, trigonometry and algebra is not only important but various mathematical tools and techniques such as logarithms and exponentials, vectors, matrix, calculus, differential and integral are also necessary for managerial economics.

3. Managerial Economics and Accounting

Various data are required by a managerial economist for the decision-making purpose. Accounting details are included in data. For example, the profit and loss statement of a firm gives details about the performance of the firm and guides the managerial economist to prepare the future course of action-whether it should improve or close down.

4. Managerial Economics and Operations Research

Models and tools of operations research or quantitative techniques are affecting the managerial economics. Operations research is a subject that consists of a number of models and analytical tools which are developed on the basis of inter-disciplinary research for solving complex problems of planning and allocation of scarce resources, primarily in defense industries.

Managerial economics has generalised and developed the models and tools of operations research for the purpose of business decision-making. Linear programming models, inventory models, game theory, etc. are a few tools that have originated in the works of operation researchers.

5. Managerial Economics and Theory of Decision-Making

Decision theory has been developed to deal with problems of choice or decision-making under uncertainty, where the applicability of figures required for the utility calculus are not available. Economic theory is based on the assumptions of a single goal whereas decision theory breaks new grounds by recognizing multiplicity of goals and persuasiveness of uncertainty in the real world of management.

6. Managerial Economics and Economics

Managerial economics has been described as economics applied to decision-making. Managerial economics has been studied as a special branch of economics, bridging the gap between pure economic theory and managerial practice. Economics has two main branches – microeconomics and macro-economics.

Major 6 Uses of Managerial Economics

1. Used for Integration of Economic Theory

Economic theory and business practice is integrated with the help of managerial economics.

2. Used as Solution to Practical Business Problems

It acts as a mean to apply economic concepts and principles to solve practical business problems in real life. Managerial economics helps in employing the most modern instruments and tools to find solutions to business problems.

3. Optimum Use of Scarce Resources

It helps in making optimum use of scarce resources of a firm to maximize profits.

4. Used for Other Objectives

The various objectives such as attaining industry leadership, expansion of market share, etc., are achieved with the help of managerial economics.

5. Used for Overall Development

Managerial economics facilitates in making overall development of a firm.

6. Used in Making Right Decisions

A manager understands the details of business problems and taking a right decision at the right time with the help of managerial economics.

Demand Forecasting

The process of predicting future demand for goods and services is known as demand forecasting. Forecasting tries to answer questions like “when,” “where,” and “how much” demand by utilizing previously collected and saved data. Forecasts can be produced using demand planning process or mathematical models based on historical data. Also, qualitative methods such as management experience or expert opinion, or a combination of the two are used to forecast demand. You must understand that predictions are not targets but educated guesses helpful in making important business decisions.

Types of demand forecasting

1. Short-term demand forecasting

Short-term forecasting is limited to three to twelve months. It will help you in supply chain management and react quickly to changes in customer demand.

2. Long-term demand forecasting

It will help you prepare for future demand by making predictions for the next one to four years. It can assist in active demand planning which is marketing campaigns, capital

investments, and internal supply chain operations. This forecasting model helps to determine the growth trajectory of your company.

3. Passive demand forecasting

Passive forecasting is the most fundamental type of forecasting. It uses past sales data to forecast the future, which is beneficial if your business has seasonal demand or fluctuations. Furthermore, this is a great model for businesses prioritizing stability over growth.

4. Active demand forecasting

It is a good option if your company is growing or starting. The active approach considers aggressive growth plans such as marketing or product development and the overall competitive environment, including the economic outlook, market growth projections, and other factors.

5. Macro demand forecasting

This model considers broader economic trends. An external macro demand forecast can address raw material availability and other factors affecting aspects of the supply chain. It will also point you in the right direction for achieving your accurate demand forecasts.

6. Internal forecasting

This forecasting model is helpful in finding out limitations and making realistic future projections. Internal demand forecasting helps to review your operations and uncover the area of opportunity within the organization. It will also help identify consumer trends so that things run smoothly to fill consumer demands

Demand-Meaning

Demand simply means a consumer's desire to buy goods and services without any hesitation and pay the price for it. In simple words, demand is the number of goods that the customers are ready and willing to buy at several prices during a given time frame. Preferences and choices are the basics of demand, and can be described in terms of the cost, benefits, profit, and other variables.

The amount of goods that the customers pick, modestly relies on the cost of the commodity, the cost of other commodities, the customer's earnings, and his or her tastes and proclivity. The amount of a commodity that a customer is ready to purchase, is able to manage and afford at provided prices of goods, and customer's tastes and preferences are known as demand for the commodity.

Determinants of Demand

There are many determinants of demand, but the top five determinants of demand are as follows:

Product cost:

Demand of the product changes as per the change in the price of the commodity. People deciding to buy a product remain constant only if all the factors related to it remain unchanged.

The income of the consumers:

When the income increases, the number of goods demanded also increases. Likewise, if the income decreases, the demand also decreases.

Costs of related goods and services:

For a complimentary product, an increase in the cost of one commodity will decrease the demand for a complimentary product. Example: An increase in the rate of bread will decrease the demand for butter. Similarly, an increase in the rate of one commodity will generate the demand for a substitute product to increase. Example: Increase in the cost of tea will raise the demand for coffee and therefore, decrease the demand for tea.

Consumer expectation:

High expectation of income or expectation in the increase in price of a good also leads to an increase in demand. Similarly, low expectation of income or low pricing of goods will decrease the demand.

Buyers in the market:

If the number of buyers for a commodity are more or less, then there will be a shift in demand.

Types of Demand

Few important different types of demand are as follows:

1. Price demand:

It refers to various types of quantities of goods or services that a customer will buy at a quoted price and given time, considering the other things remain constant.

2. Income demand:

It refers to various types of quantities of goods or services that a customer will buy at different stages of income, considering the other things remain constant.

3. Cross demand:

This means that the product's demand does not depend on its own cost but depends on the cost of the other related commodities.

4. **Direct demand:**

When goods or services satisfy an individual's wants directly, it is known as direct demand.

5. **Derived demand or Indirect demand:**

The goods or services demanded or needed for manufacturing the goods and satisfying the consumer indirectly is known as derived demand.

6. **Joint demand:**

To produce a product there are many things that are related to each other, for example, to produce bread, we need services like an oven, fuel, flour mill, and more. So, the demand for other additional things to produce a product is known as joint demand.

7. **Composite demand:**

A composite demand can be described when goods and services are utilised for more than one cause. Example: Coal

Break Even Analysis

A break-even analysis is an economic tool that is used to determine the cost structure of a company or the number of units that need to be sold to cover the cost. Break-even is a circumstance where a company neither makes a profit nor loss but recovers all the money spent.

The break-even analysis is used to examine the relation between the fixed cost, variable cost, and revenue. Usually, an organisation with a low fixed cost will have a low break-even point of sale.

Importance of Break-Even Analysis

Manages the size of units to be sold:

With the help of break-even analysis, the company or the owner comes to know how many units need to be sold to cover the cost. The variable cost and the selling price of an individual product and the total cost are required to evaluate the break-even analysis.

Budgeting and setting targets:

Since the company or the owner knows at which point a company can break-even, it is easy for them to fix a goal and set a budget for the firm accordingly. This analysis can also be practised in establishing a realistic target for a company.

Manage the margin of safety:

In a financial breakdown, the sales of a company tend to decrease. The break-even analysis helps the company to decide the least number of sales required to make profits. With the margin of safety reports, the management can execute a high business decision.

Monitors and controls cost:

Companies' profit margin can be affected by the fixed and variable cost. Therefore, with break-even analysis, the management can detect if any effects are changing the cost.

Helps to design pricing strategy:

The break-even point can be affected if there is any change in the pricing of a product. For example, if the selling price is raised, then the quantity of the product to be sold to break-even will be reduced. Similarly, if the selling price is reduced, then a company needs to sell extra to break-even.

Components of Break-Even Analysis

- **Fixed costs:**

These costs are also known as overhead costs. These costs materialise once the financial activity of a business starts. The fixed prices include taxes, salaries, rents, depreciation cost, labour cost, interests, energy cost, etc.

- **Variable costs:**

These costs fluctuate and will decrease or increase according to the volume of the production. These costs include packaging cost, cost of raw material, fuel, and other materials related to production.

Uses of Break-Even Analysis

- **New business:**

For a new venture, a break-even analysis is essential. It guides the management with pricing strategy and is practical about the cost. This analysis also gives an idea if the new business is productive.

- **Manufacture new products:**

If an existing company is going to launch a new product, then they still have to focus on a break-even analysis before starting and see if the product adds necessary expenditure to the company.

- **Change in business model:**

The break-even analysis works even if there is a change in any business model like shifting from retail business to wholesale business. This analysis will help the company to determine if the selling price of a product needs to change

Economies of Scale

Economies of scale refer to the cost advantage experienced by a firm when it increases its level of output. The advantage arises due to the inverse relationship between the per-unit fixed cost and the quantity produced. The greater the quantity of output produced, the lower the per-unit fixed cost.

Economies of scale also result in a fall in average variable costs (average non-fixed costs) with an increase in output. This is brought about by operational efficiencies and synergies as a result of an increase in the scale of production.

Economies of scale can be realized by a firm at any stage of the production process. In this case, production refers to the economic concept of production and involves all activities related to the commodity, not involving the final buyer.

Thus, a business can decide to implement economies of scale in its marketing division by hiring a large number of marketing professionals. A business can also adopt the same in its input sourcing division by moving from human labor to machine labour.

Effects of Economies of Scale on Production Costs

1. It reduces the per-unit fixed cost. As a result of increased production, the fixed cost gets spread over more output than before.
2. It reduces per-unit variable costs. This occurs as the expanded scale of production increases the efficiency of the production process.

Types of Economies of Scale

1. Internal Economies of Scale

This refers to economies that are unique to a firm. For instance, a firm may hold a patent over a mass production machine, which allows it to lower its average cost of production more than other firms in the industry.

2. External Economies of Scale

These refer to economies of scale enjoyed by an entire industry. For instance, suppose the government wants to increase steel production. In order to do so, the government announces that all steel producers who employ more than 10,000 workers will be given a 20% tax break.

Thus, firms employing less than 10,000 workers can potentially lower their average cost of production by employing more workers. This is an example of an external economy of scale – one that affects an entire industry or sector of the economy.

Sources of Economies of Scale

1. Purchasing

Firms might be able to lower average costs by buying the inputs required for the production process in bulk or from special wholesalers. By negotiating with suppliers for volume discounts, the purchasing firm takes advantage of economies of scale.

2. Managerial

Firms might be able to lower average costs by improving the management structure within the firm. The firm might hire better skilled or more experienced managers.

3. Technological

A technological advancement might drastically change the production process. For instance, fracking completely changed the oil industry a few years ago. However, only large oil firms that could afford to invest in expensive fracking equipment could take advantage of the new technology.

Definition of National Income

The total net value of all goods and services produced within a nation over a specified period of time, representing the sum of wages, profits, rents, interest, and pension payments to residents of the nation.

Measures of National Income

The purpose of measurement and analysis, national income can be viewed as an aggregate of various component flows. The most comprehensive measure of aggregate income which is widely known is Gross National Product at market prices.

Gross and Net Concept

Gross emphasizes that no allowance for capital consumption has been made or that depreciation has yet to be deducted. Net indicates that provision for capital consumption has already been made or that depreciation has already been deducted.

National and Domestic Concepts

The term national denotes that the aggregate under consideration represents the total income which accrues to the normal residents of a country due to their participation in world production during the current year.

It is also possible to measure the value of the total output or income originating within the specified geographical boundary of a country known as domestic territory. The resulting measure is called "domestic product".

Market Prices and Factor Costs

The valuation of the national product at market prices indicates the total amount actually paid by the final buyers while the valuation of national product at factor cost is a measure of the total amount earned by the factors of production for their contribution to the final output.

$$\text{GNP at market price} = \text{GNP at factor cost} + \text{indirect taxes} - \text{Subsidies.}$$

$$\text{NNP at market price} = \text{NNP at factor cost} + \text{indirect taxes} - \text{Subsidies}$$

Gross National Product and Gross Domestic Product

For some purposes we need to find the total income generated from production within the territorial boundaries of an economy irrespective of whether it belongs to the inhabitants of that nation or not. Such an income is known as Gross Domestic Product (GDP) and found as –

$$\text{GDP} = \text{GNP} - \text{Net Factor Income From Abroad}$$

Net Factor Income from Abroad = Factor Income Received From Abroad - Factor Income Paid Abroad

Net National Product

The NNP is an alternative and closely related measure of the national income. It differs from GNP in only one respect. GNP is the sum of final products. It includes consumption of goods, gross investment, government expenditures on goods and services, and net exports.

$$\text{GNP} = \text{NNP} - \text{Depreciation}$$

NNP includes net private investment while GNP includes gross private domestic investment.

Personal Income

Personal income is calculated by subtracting from national income those types of incomes which are earned but not received and adding those types which are received but not currently earned.

Personal Income = NNP at Factor Cost – Undistributed Profits – Corporate Taxes + Transfer Payments

Disposable Income

Disposable income is the total income that actually remains with individuals to dispose off as they wish. It differs from personal income by the amount of direct taxes paid by individuals.

$$\text{Disposable Income} = \text{Personal Income} - \text{Personal taxes}$$

Value Added

The concept of value added is a useful device to find out the exact amount that is added at each stage of production to the value of the final product. Value added can be defined as the difference between the value of output produced by that firm and the total expenditure incurred by it on the materials and intermediate products purchased from other business firms.

Methods of Measuring National Income

Product Approach

In product approach, national income is measured as a flow of goods and services. Value of money for all final goods and services is produced in an economy during a year. Final goods are those goods which are directly consumed and not used in further production process. In our economy product approach benefits various sectors like forestry, agriculture, mining etc to estimate gross and net value.

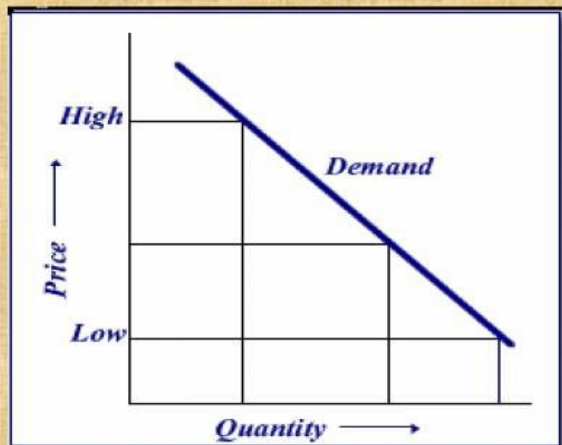
Income Approach

In income approach, national income is measured as a flow of factor incomes. Income received by basic factors like labor, capital, land and entrepreneurship are summed up. This approach is also called as income distributed approach.

Expenditure Approach

This method is known as the final product method. In this method, national income is measured as a flow of expenditure incurred by the society in a particular year. The expenditures are classified as personal consumption expenditure, net domestic investment, government expenditure on goods and services and net foreign investment.

Demand



Demand for a particular product or service represents how much people are willing to purchase at various prices.

Demand is represented graphically as a downward sloping curve with price on the vertical axis and quantity on the horizontal axis

Law of Demand

Law of Demand states that if price of commodity increases quantity demanded will fall and if price of commodity falls quantity will increase.

Law of demand indicates only direction of change in quantity demanded in response to change in price but **ELASTICITY OF DEMAND** states with how much or to what extent the quantity demanded will change in response to change in any determinants.

Meaning & Definition of Elasticity of Demand

Elasticity of Demand measures the extent to which quantity demanded of a commodity increases or decreases in response to increase or decrease in any of its quantitative determinants.

So, we have several types of elasticity of demand according to the source of the change in the demand. For example, if the price is the source of the change, we have the "price elasticity of demand".

"The elasticity (or responsiveness) of demand in a market is great or small according as the amount demanded increases much or little for a given fall in price, and diminishes much or little for a given rise in price". – Dr. Marshall.

Elasticity of Demand

According to the source of the change, the following types of elasticity of demand can be mentioned:

- Price Elasticity of Demand
- Cross Elasticity of Demand (the elasticity in relation to the change of the price of other good and services)
- Income Elasticity of Demand
- Advertisement Elasticity of Demand (the elasticity in relation to the advertisement expenditure)

According to the degree of the change in the demand, the elasticity can be classified in:

- Perfectly Elastic
- Relatively Elastic
- Unitary Elasticity
- Relatively Inelastic
- Perfect Inelastic

Price Elasticity of Demand

Price Elasticity of demand is a measurement of percentage change in demand due to percentage change in own price of the commodity.

The price elasticity of Demand may be defined as the ratio of the relative change in demand and price variables.

$$e = \frac{\text{Percentage/Proportional Change in Quantity Demanded}}{\text{Percentage/Proportional Change in Price}}$$

Degree of Price Elasticity of Demand

Five cases of elasticity of demand are studied depending upon their degree:

- Perfectly Elastic
- Perfectly Inelastic
- Unitary Elastic
- Relatively Elastic
- Relatively Inelastic

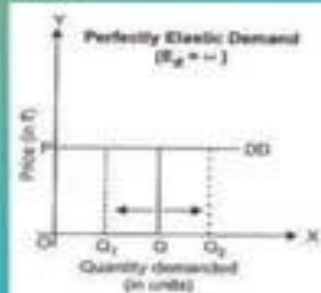
Perfectly Elastic Demand

When a small change in price of a product causes a major change in its demand, it is said to be perfectly elastic demand. In perfectly elastic demand, a small rise in price results in fall in demand to zero, while a small fall in price causes increase in demand to infinity.

A perfectly elastic demand refers to the situation when demand is infinite at the prevailing price.

In perfectly elastic demand, a small rise in price results in fall in demand to zero, while a small fall in price causes increase in demand to infinity.

The degree of elasticity of demand helps in defining the shape and slope of a demand curve. Therefore, the elasticity of demand can be determined by the slope of the demand curve. **Flatter the slope of the demand curve, higher the elasticity of demand.**



Perfectly Inelastic Demand

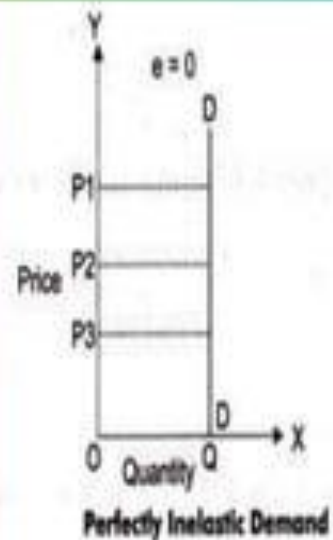
A Perfectly inelastic demand is one in which a change in price causes no change in quantity demanded.

It is a situation where even substantial changes in price leave the demand unaffected.

It can be interpreted from Figure that the movement in price from OP₁ to OP₂ and OP₂ to OP₃ does not show any change in the demand of a product (OQ).

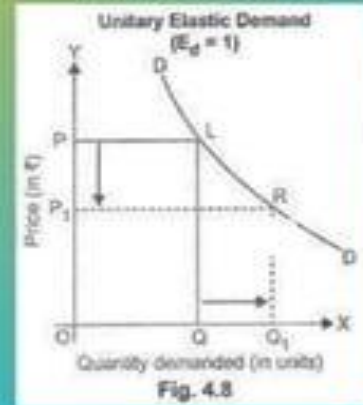
The demand remains constant for any value of price.

Perfectly inelastic demand is a theoretical concept and cannot be applied in a practical situation. However, in case of essential goods, such as salt, the demand does not change with change in price. Therefore, the demand for essential goods is perfectly inelastic.



Unitary Elastic Demand

- When the proportionate change in demand produces the same change in the price of the product, the demand is referred as unitary elastic demand. The numerical value for unitary elastic demand is equal to one ($e_p=1$).
- The demand curve for unitary elastic demand is represented as a rectangular hyperbola.

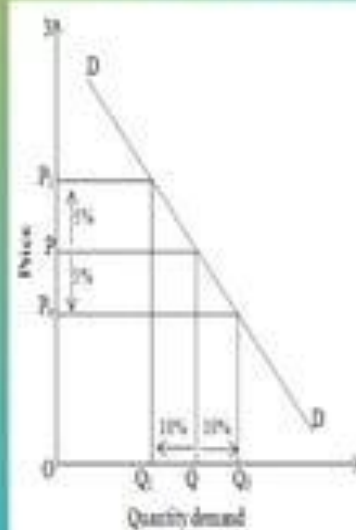


Relatively Elastic Demand

Relatively elastic demand refers to the demand when the proportionate change produced in demand is greater than the proportionate change in price of a product.

Mathematically, relatively elastic demand is known as more than unit elastic demand ($e_p > 1$). For example, if the price of a product increases by 20% and the demand of the product decreases by 25%, then the demand would be relatively elastic.

In this the demand is more responsive to the change in price



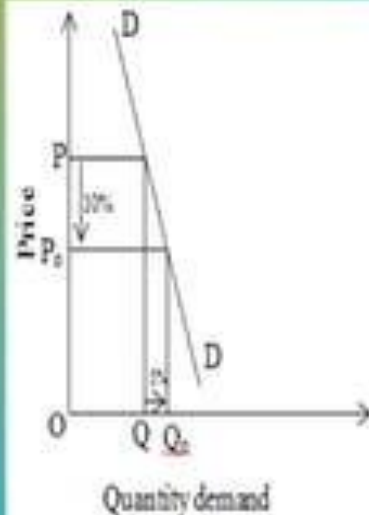
Relatively Inelastic Demand

Relatively inelastic demand is one when the percentage change produced in demand is less than the percentage change in the price of a product.

For example, if the price of a product increases by 30% and the demand for the product decreases only by 10%, then the demand would be called relatively inelastic.

The numerical value of relative elastic demand ranges between zero to one ($e_p < 1$).

Marshall has termed relatively inelastic demand as elasticity being less than unity.



DEFINITIONS

- **Cost Control** is a process which focuses on controlling the total cost through competitive analysis.
- **Cost Reduction** is a process, aims at lowering the unit cost of a product manufactured or service rendered without affecting its quality by using new and improved methods and techniques.

TECHNIQUES OF COST REDUCTION

- Material Handling
- Automation
- Production Control
- Work study
- Design

BASIS FOR COMPARISON	COST CONTROL	COST REDUCTION
Meaning	A technique used for maintaining the costs as per the set standards is known as Cost Control.	A technique used to economize the unit cost without lowering the quality of the product is known as Cost Reduction.
Savings in	Total Cost	Cost Per Unit
Retention of Quality	Not Guaranteed	Guaranteed
Nature	Temporary	Permanent
Emphasis on	Past and Present Cost	Present and Future Cost
Ends when	The pre-determined target is achieved.	No end
Type of Function	Preventive	Corrective

INTRODUCTION

- A **breakeven analysis** is used to determine how much sales volume your business needs to start making a profit.
- The breakeven analysis is especially useful when you're developing a pricing strategy, either as part of a marketing plan or a business plan.
- In economics & business, specifically cost accounting, the **break-even point** (BEP) is the point at which cost or expenses and revenue are equal; there is no net loss or gain, and one has "broken even".
- $\text{Total cost} = \text{Total revenue} = \text{B.E.P.}$

BREAK EVEN ANALYSIS

In order to calculate how profitable a product will be, we must firstly look at the Costs, Price and Revenue involved.

- There are two basic types of costs a company incurs.
 - **Variable Costs**
 - **Fixed Costs**
- **Variable costs** are costs that change with changes in production levels or sales. Examples include: Costs of materials used in the production of the goods.
- **Fixed costs** remain roughly the same regardless of sales/output levels. Examples include: Rent, Insurance and Wages

ASSUMPTIONS

- All elements of cost i.e. production, administration and selling distribution can be divided into fixed and variable components.
- Variable costs remain constant per unit of output.
- Fixed cost remain constant at all volume of output.
- Selling price per unit remains unchanged or constant at all levels of output.
- Volume of production is the only factor that influences cost.
- There will be no change in the general price level.
- There is one product and in case of multi product, the sales remain constant.

MARGIN OF SAFETY

- Margin of safety represents the strength of the business. It enables a business to know what is the exact amount it has gained or lost and whether they are over or below the break even point.
- margin of safety = (current output – breakeven output) OR
- Margin of safety = actual sales – BEP sales
- margin of safety% = $(\text{current output} - \text{breakeven output}) / \text{current output} \times 100$

USES OF BREAK EVEN POINT

- Helpful in deciding the minimum quantity of sales
- Helpful in the determination of tender price.
- Helpful in examining effects upon organization's profitability.
- Helpful in deciding about the substitution of new plants.
- Helpful in sales price and quantity.
- Helpful in determining marginal cost.

LIMITATIONS

- Break-even analysis is only a supply side (costs only) analysis, as it tells you nothing about what sales are actually likely to be for the product at these various prices.
- It assumes that fixed costs (FC) are constant
- It assumes average variable costs are constant per unit of output, at least in the range of likely quantities of sales.
- It assumes that the quantity of goods produced is equal to the quantity of goods sold (i.e., there is no change in the quantity of goods held in inventory at the beginning of the period and the quantity of goods held in inventory at the end of the period.
- In multi-product companies, it assumes that the relative proportions of each product sold and produced are constant.

QUESTION BANK

1. Explain the role and responsibilities of the Managerial Economist.
2. Discuss the uses of Managerial Economics.
3. Discuss the uses of Managerial Economics.
4. What is Demand forecasting? Explain its types.
5. Describe the determinants of demand.
6. Discuss the cost output relationship in the short run.
7. Describe the assumptions of production function.
8. Discuss the types of oligopoly
9. Explain the features of perfect competition.
10. Write a short note on percapita Income.
11. Explain the significance of National Income.