Rohini Engineering college and Technology,Palkulam

UNIT- I

LESSON 1 **MANAGERIAL ECONOMICS**

STRUCTURE

1.1 INTRODUCTION

The science of Managerial Economics has emerged only recently. With the growing variabilityand unpredictabilityof the business environment, business managers have become increasingly concerned with finding rational and ways of adjusting to an exploiting environmental change. The problems of the business world attracted the attentions of the academicians from 1950 onwards. Mana-gerial economics as a subject gained popularity in the USA after the publication of the book "Managerial Economics" by Joel Dean in 1951.

Managerial Economics can be defined as amalgamation of economic theory with business practices so as to ease decision-making and future planning by management. Managerial Economics assists the managers of a firm in a rational solution of obstacles faced in the firm's activities. It makes use of economic theory and concepts. It helps in formulating logical managerial decisions. The key of Managerial Economics is the micro-economic theory of the firm. It lessens the gap between economics in theory and economics in practice. Managerial Economics is a science dealing with effective use of scarce resources. It guides the managers in taking decisions relating to the firm's customers, competitors, suppliers as well as relating to the internal functioning of a firm. It makes use of statistical and analytical tools to assess economic theories in solving practical business problems. Study of Managerial Economics helps in enhancement of analytical skills, assists in rational configuration as well as solution of problems. While microeconomics is the study of decisions made regarding the allocation of resources and prices of goods and services, macroeconomics is the field of economics that studies the behaviour of the economy as a whole (i.e. entire industries and economies).

The following figure tells the primary ways in which Managerial Economics correlates to managerial decision-making.

1.1.2 DEFINITION:

Managerial economists have defined managerial economics in a variety of ways:

According to E.F. Brigham and J. L. Pappar, Managerial Economics is "The application of economic theory and methodology to business administration practice."

Christopher Savage and John R. Small: "Managerial Economics is concerned with business efficiency".

Milton H. Spencer and Lonis Siegelman define Managerial Economics as "The integration of eco-nomic theory with business practice for the purpose of facilitating decision making and forward plan-ning by management."

In the words of Me *Nair and Meriam*, "Managerial Economics consists of the use of economic modes of thought to analyse business situations."

D.C. Hague describes Managerial Economics as "A fundamental academic subject which seeks to understand and analyse the problems of business decision making."

In the opinion of *W.W. Haynes* "Managerial Economics is the study of the allocation of resources available to a firm of other unit of management among the activities of that unit."

According to Floyd E. Gillis, "Managerial Economics deals almost exclusively with those busi-ness situations that can be quantified and dealt with in a model or at least approximated quantitatively."

1.2 OBJECTIVES

The objectives of this lesson is:

- To understand the concept of managerial economics.
- To know the scope and importance of managerial economics.

1.3 NATURE OF MANAGERIAL ECONOMICS

Managers studymanagerial economics because it gives them insight to reign the functioning of the organisation. If manager uses the principles applicable to economic behaviour reasonably, then it will result in smooth functioning of the organisation.

1.3.1 Managerial Economics is a Science

Managerial Economics is an essential scholastic field. It can be compared to science in a sense that it fulfills the criteria of being a science in following sense:

- Science is a Systematic body of Knowledge. It is based on the methodical observation. Managerial economics is also a science of making decisions with regard to scarce resources with alternative applications. It is a body of knowledge that determines or observes the internal and external environment for decision making.
- In science any conclusion is arrived at after continuous experimentation. In

Managerial economics also policies are made after persistent testing and trailing. Though economic environment consists of human variable, which is unpredictable, thus the policies made are not rigid. Managerial economist takes decisions by utilising his valuable past experience and observations.

- Science principles are universally applicable. Similarly policies of Managerial economics are also universally applicable partially if not fully. The policies need to be changed from time to time depending on the situation and attitude of individuals to those particular situations. Policies are applicable universally but modifications are required periodically.

1.3.2 Managerial Economics requires Art

Managerial economist is required to have an art of utilising his capability, knowledge and understanding to achieve the organizational objective. Managerial economist should have an art to put in practice his theoretical knowledge regarding elements of economic environment.

1.3.3 Managerial Economics for administration of organisation

Managerial economics helps the management in decision making. These decisions are based on the economic rationale and are valid in the existing economic environment.

1.3.4 Managerial economics is helpful in optimum resource allocation

The resources are scarce with alternative uses. Managers need to use these limited resources optimally. Each resource has several uses. It is manager who decides with his knowledge of economics that which one is the preeminent use of the resource.

1.3.5 Managerial Economics has components of micro economics

Managers studyand manage the internal environment of the organization and work for the profitable and long-term functioning of the organisation. This aspect refers to the micro economics study. The managerial economics deals with the problems faced by the individual organization such as main objective of the organisation, demand for its product, price and output determination of the organisation, available substitute and complimentary goods, supply of inputs and raw material, target or prospective consumers of its products etc.

1.3.6 Economics has components of macro economics

None of the organisation works in isolation. They are affected by the external environment of the economy in which it operates such as government policies, general price level, income and employment levels in the economy, stage of business cycle in which economy is operating, exchange rate, balance of payment, general expenditure, saving and investment patterns of the consumers, market conditions etc. These aspects are related to macro economics.

1.3.7 Managerial Economics is dynamic in nature

Managerial Economics deals with human-beings (i.e. human resource, consumers, producers etc.). The nature and attitude differs from person to person. Thus to cope up with dynamism and vitality managerial economics also changes itself over a period of time.

1.4 IMPORTANCE OF MANAGERIAL ECONOMICS

The significance or importance of business/managerial economics can be discussed as:

1. Business economics is concerned with those aspects of traditional economics which are relevant for business decision making in real life. These are adapted or modified with a view to enable the manager take better decisions. Thus, business economic accomplishes the objective of building a suitable tool kit from traditional economics.

2. It also incorporates useful ideas from other disciplines such as psychology, sociology, etc. If they are found relevant to decision making. In fact, business economics takes the help of other disciplines having a bearing on the business decisions in relation various explicit and implicit constraints subject to which resource allocation is to be optimised.

3. Business economics helps in reaching a variety of business decisions in a complicated environment. Certain examples are:

   (i) What products and services should be produced?

   (ii) What input and production technique should be used?

   (iii) How much output should be produced and at what prices it should be sold?

(iv) What are the best sizes and locations of new plants?

(v) When should equipment be replaced?

(vi) How should the available capital be allocated?

4. Business economics makes a manager a more competent model builder. It helps him appreciate the essential relationship Characterising a given situation.

5. At the level of the firm. Where its operations are conducted though known focus functional areas, such as finance, marketing, personnel and production, business economics serves as an integrating agent by coordinating the activities in these different areas.

6. Business economics takes cognizance of the interaction between the firm and society, and accomplishes the key role of an agent in achieving the its social and economic welfare goals. It has come to be realised that a business, apart from its obligations to shareholders, has certain social obligations. Business economics focuses attention on these social obligations as constraints subject to which business decisions are taken. It serves as an instrument in furthering the economic welfare of the societythrough socially oriented business decisions.

1.5 SCOPE OF MANAGERIAL ECONOMICS

Managerial Economics is a developing subject. The scope of managerial economics refers to its area of study. Managerial economics has its roots in economic theory. The empirical nature of managerial economics makes its scope wider. Managerial economics provides management with strategic planning tools that can be used to get a clear perspective of the way the business world works and what can be done to maintain profitability in an ever changing environment. Managerial economics refers to those aspects of economic theory and application which are directly relevant to the practice of manage-ment and the decision making process within the enterprise. Its scope does not extend to macro-eco-nomic theory and the economics of public policy which will also be of interest to the manager.

While considering the scope of managerial economics we have to understand whether it is positive economics or normative economics.

1.5.1 Positive versus Normative Economics:

Most of the managerial economists are of the opinion that managerial economics is fundamentally normative and prescriptive in nature. It is concerned with what decisions ought to be made. The applica-tion of managerial economics is inseparable from consideration of values or norms, for it is always concerned with the achievement of objectives or the optimisation of goals. In managerial economics, we are interested in what should happen rather than what does happen. Instead of explaining what a firm is doing, we explain what it should do to make its decision effective.

I. Positive Economics:

A positive science is concerned with 'what is'. Robbins regards economics as a pure science of what is, which is not concerned with moral or ethical questions. Economics is neutral between ends. The economist has no right to pass judgment on the wisdom or folly of the ends itself. He is simply concerned with the problem of resources in relation to the ends desired. The manufacture and sale of cigarettes and wine may be injurious to health and therefore morally unjustifiable, but the economist has no right to pass judgment on these since both satisfy human wants and involve economic activity.

II. Normative Economics:

Normative economics is concerned with describing what should be the things. It is, therefore, also called prescriptive economics. What price for a product should be fixed, what wage should be paid, how income should be distributed and so on, fall within the purview of normative economics?

It should be noted that normative economics involves value judgments.Almost all the leading managerial econo-mists are of the opinion that managerial economics is fundamentally normative and prescriptive in nature. It refers mostly to what ought to be and cannot be neutral about the ends. The application of managerial economics is inseparable from consideration of values, or norms for it is always concerned with the achievement of objectives or the optimisation of goals.

Further, in managerial economics, we are interested in what should happen rather than what does happen. Instead of explaining what a firm is doing, we explain what it should do to make its decision effective. Managerial economists are generally preoccupied with the optimum allocation of scarce resources among competing ends with a view to obtaining the maximum benefit according to predetermined criteria.

To achieve these objectives they do not assume ceteris paribus, but try to introduce policies. The very important aspect of managerial economics is that it tries to find out the cause and effect relationship by factual study and logical reasoning. The scope of managerial economics is so wide that it embraces almost all the problems and areas of the manager and the firm.

1.5.2 Subject Matter of Marginal Economics

1. Demand Analysis and Forecasting

A firm is an economic organisation which transforms inputs into output that is to be sold in a market. Accurate estimation of demand, by analysing the forces acting on demand of the product produced by the firm, forms the vital issue in taking effective decision at the firm level. A major part of managerial decision making depends on accurate estimates of demand. When demand is estimated, the manager does not stop at the stage of assessing the current demand but estimates future demand as well. This is what is meant by demand forecasting. This forecast can also serve as a guide to management for maintaining or strengthening market position and enlarging profit. Demand analysis helps in identifying the various factors influencing the demand for a firm's product and thus provides guidelines to manipu-late demand. The main topics covered are: Demand Determinants, Demand Distinctions and Demand Forecasting.

2. Cost and Production Analysis

Cost analysis is yet another function of managerial economics. In decision making, cost estimates are very essential. The factors causing variation in costs must be recognised and allowed for if management is to arrive at cost estimates which are significant for planning purposes.

The determinants of estimating costs, the relationship between cost and output, the forecast of cost and profit are very vital to a firm. An element of cost uncertainty exists because all the factors determining costs are not always known or controllable. Managerial economics touches these aspects of cost analysis as an effective knowledge and the application of which is corner stone for the success of a firm.

Production analysis frequently proceeds in physical terms. Inputs play a vital role in the economics of production. The factors of production otherwise called inputs, may be combined in a particular way to yield the maximum output.

Alternatively, when the price of inputs shoots up, a firm is forced to work out a combination of inputs so as to ensure that this combination becomes the least cost combination. The main topics covered under cost and production analysis are production function, least cost combination of factor inputs, factor productiveness, returns to scale, cost concepts and classification, cost-output relationship and linear programming.

3. Inventory Management

An inventory refers to a stock of raw materials which a firm keeps. Now the problem is how much of the inventoryis the ideal stock. If it is high, capital is unproductively tied up. If the level of inventory is low, production will be affected.

Therefore, managerial economics will use such methods as Economic Order Quantity (EOQ) approach, ABC analysis with a view to minimising the inventory cost. It also goes deeper into such aspects as motives of holding inventory, cost of holding inventory, inventory control, and main methods of inventory control and management.

4. Advertising

To produce a commodity is one thing and to market it is another. Yet the message about the product should reach the consumer before he thinks of buying it. Therefore, advertising forms an integral part of decision making and forward planning. Expenditure on advertising andrelated types of promotional activities is called selling costs byeconomists.

There are different methods for setting advertising budget: Percentage of Sales Approach, All You can Afford Approach, Competitive Parity Approach, Objective and Task Approach and Return on Investment Approach.

5. Pricing Decision, Policies and Practices

Pricing is very important area of managerial economics. The control functions of an enterprise are not only productions but pricing as well. When pricing a commodity, the cost of production has to be taken into account. Business decisions are greatly influenced by pervading market structure and the structure of markets that has been evolved by the nature of competition existing in the market.

Pricing is actually guided by consideration of cost plan pricing and the policies of public enterprises. The knowledge of the pricing of a product under conditions of oligopoly is also essential. The price system guides the manager to take valid and profitable decision.

6. Profit Management

A business firm is an organisation designed to make profits. Profits are acid test of the individual firm's performance. In appraising a company, we must first understand how profit arises. The concept of profit maximisation is very useful in selecting the alternatives in making a decision at the firm level.

Profit forecasting is an essential function of anymanagement. It relates to projection of future earnings and involves the analysis of actual and expected behaviour of firms, the sales volume, prices and competitor's strategies, etc. The main aspects covered under this area are the nature and measurement of profit, and profit policies of special significance to managerial decision making.

Managerial economics tries to find out the cause and effect relationship by factual study and logical reasoning. For example, the statement that profits are at a maximum when marginal revenue is equal to marginal cost, a substantial part of economic analysis of this deductive proposition attempts to reach specific conclusions about what should be done.

The logic of linear programming is deduction of mathematical form. In fine, managerial economics is a branch of normative economics that draws from descriptive economics and from well established deductive patterns of logic.

7. Capital Management

Planning and control of capital expenditures is the basic executive function. The managerial problem of planning and control of capital is examined from an economic stand point. The capital budgeting process takes different forms in different industries.

It involves the equi-marginal principle. The objective is to assure the most profitable use of funds, which means that funds must not be applied when the managerial returns are less than in other uses. The main topics dealt with are: Cost of Capital, Rate of Return and

Selection of Projects.

Thus we see that a firm has uncertainties to rock on with. Therefore, we can conclude that the subject matter of managerial economics consists of applying economic principles and concepts towards adjusting with these uncertainties of the firm.

In recent years, there is a trend towards integration of managerial economics and Operation Research. Hence, techniques such as linear Programming, Inventory Models, Waiting Line Models, Bidding Models, Theory of Games, etc. have also come to be regarded as part of managerial economics.

1.5.3 Relation to Other Branches of Knowledge

A useful method of throwing light on the nature and scope of managerial economics is to examine its relationship with other disciplines. To classify the scope of a field of study is to discuss its relation to other subjects. If we take the subject in isolation, our study would not be useful. Managerial economics has a close linkage with other disciplines and fields of study.

The subject has gained bythe interaction with economics, mathematics and statistics and has drawn upon management theory and accounting concepts. The managerial eco-nomics integrates concepts and methods from these disciplines and bringing them to bear on managerial problems.

(i) Managerial Economics and Economics:

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

Micro-economics:

'Micro' means small. It studies the behaviour of the individual units and small groups of such units. It is a study of particular firms, particular households, individual prices, wages, incomes, individual industries and particular commodities. Thus micro-economics gives a microscopic view of the economy.

The micro-economic analysis may be undertaken at three levels:

(i) The equalisation of individual consumers and produces;

(ii) The equalisation of the single market;

(iii) The simultaneous equilibrium of all markets. The problems of scarcity and optimal or ideal allocation of resources are the central problem in micro-economics.

The roots of managerial economics spring from micro-economic theory. In price theory, demand concepts, elasticity of demand, marginal cost marginal revenue, the short and long runs and theories of market structure are sources of the elements of micro-economics which managerial economics draws upon. It also makes use of well known models in price theory such as the model for monopoly price, the kinked demand theory and the model of price discrimination.

Macro-economics:

'Macro' means large. It deals with the behaviour of the large aggregates in the economy. The large aggregates are total saving, total consumption, total income, total employment, general price level, wage level, cost structure, etc. Thus macro-economics is aggregative economics.

It examines the interrelations among the various aggregates, and causes of fluctuations in them. Problems of determination of total income, total employment and general price level are the central problems in macro-economics.

Macro-economies is also related to managerial economics. The environment, in which a business operates, fluctuations in national income, changes in fiscal and monetary measures and variations in the level of business activityhave relevance to business decisions. The understanding of the overall opera-tion of the economic system is very useful to the managerial economist in the formulation of his policies.

The chief contribution of macro-economics is in the area of forecasting. The post-Keynesian aggregative theory has direct implications for forecasting general business conditions. Since the prospects of an individual firm often depend greatly on business in general, forcasts of an individual firm depend on general business forecasts, which make use of models derived from theory. The most widely used model in modern forecasting is the gross national product model.

(ii) Managerial Economics and Theory of Decision Making:

The theory of decision making is a relatively new subject that has a significance for managerial economics. In the entire process of management and in each of the management activities such as planning, organising, leading and controlling, decision making is always essential. In fact, decision making is an integral part of today's business management. A manager faces a number of problems connected with his/her business such as production, inventory, cost, marketing, pricing, investment and personnel.

Economist are interested in the efficient use of scarce resources hence they are naturally interested in business decision problems and theyapplyeconomics in management of business problems. Hence managerial economics is economics applied in decision making. According to M.H. Spencer and L. Siegelman, "Managerial economics is the integration of economic theorywith business practice for the purpose of facilitating decision making up and forward planning bymanagement". Managerial economics is a fundamental academic subject which seeks to understand and to analyse the problems of busi-ness decision making.

The theory of decision making recognises the multiplicity of goals and the pervasiveness of uncertainty in the real world of management. The theory of decision making replaces the notion of a single optimum solution with the view that the objective is to find solution that 'satisfies' rather than maximise. It probes into an analysis of motivation of the relation of rewards and aspiration levels, and of pattern of influence and authority.

Economic theory and theory of decision making appear to be in conflict, each based on different set of assumptions. Much of the economic theory is based on the assumption of single goal-maximisation of utility for the individual or maximisation of profit for the firm.

(iii) Managerial Economics and Operations Research:

Mathematicians, statisticians, engineers and others teamed up together and developed models and analytical tools which have since grown into a specialised subject, known as operation research. The basic purpose of the approach is to develop a scientific model of the system which may be utilised for policy making.

Much of the development of techniques and concepts such as Linear Programming, Dynamic Programming, Input-output Analysis, Inventory Theory, Information Theory, Probability Theory, Queueing Theory, Game Theory, Decision Theory and Symbolic Logic.

Linear programming deals with those programming problems where the relationship among the variables is linear. It is a useful tool for the managerial economist for reducing transportation costs and allocating purchase amongst different supplies and site depots. It is employed when the objective func-tion is to maximise profit, output or efficiency.

Dynamic programming helps in solving certain types of sequential decision problems. A sequen-tial decision problem is one in which a sequence of decision must be made with each decision affecting future decision. It has been applied in cases of maintenance and repair, financial portfolio balancing, inventory and production control, equipment replacement and directed marketing.

Input-output analysis is a technique for analysing inter-industry relation. Prof. W.W. Leontief tries to establish inter industry relationships by dividing the economy into different sectors. In this model, the final demand is treated as exogenously determined and the input-output technique is used to find out the levels of activity in the various sectors of the economic system. It can be used by firms for planning, co-ordination and mobilisation of resources.

Queueing is a particular application of the statistical decision theory. It is employed to get the optimum solution. The theory may be applied to such problems as how to meet a given demand most economically or how to minimise the waiting period or idle time. The theory of games holds out the hope of solving certain problems concerning oligopolistic interminacy.

When we apply the game theory, we have to consider the following:

(i) The players are the two firms;

(ii) They play the game in the market place;

(iii) Their strategies are their price or output decision; and

(iv) The pay-offs or rewards are their profits. The numerical figures are what is called pay-off matrix. This matrix is the most important tool of game theory.

(iv) Managerial Economics and Statistics:

Statistics is important to managerial economics. It provides the basis for the empirical testing of theory. Statistics is important in providing the individual firm with measures of the appropriate func-tional relationship involved in decision making. Statistics is a very useful science for business executives because a business runs on estimates and probabilities.

Statistics supplies many tools to managerial economics. Suppose forecasting has to be done. For this purpose, trend projections are used. Similarly, multiple regression technique is used. In managerial economics, measures of central tendency like the mean, median, mode, and measures of dispersion, correlation, regression, least square, estimators are widely used. The managerial economics is con-stantly faced with the choice between models ignoring uncertainty and those that explicitly incorporate probability theory.

Statistical tools are widely used in the solution of managerial problems. For example, sampling is very useful in data collection. Managerial economics makes use of correlation and multiple regression in business problems involving some kind of cause and effect relationship.

(v) Managerial Economics and Accounting:

Managerial economics is closely related to accounting. It is concerned with recording the financial operation of a business firm. Abusiness is started with the main aim of earning profit. Capital is invested it is employed for purchasing properties such as building, furniture, etc and for meeting the current expenses of the business.

Goods are bought and sold for cash as well as credit. Cash is paid to credit sellers. It is received from credit buyers. Expenses are met and incomes derived. This goes on the daily routine work of the business. The buying of goods, sale of goods, payment of cash, receipt of cash and similar dealings are called business transactions.

The business transactions are varied and multifarious. They are too numerous to be kept in one’s memory. This has given rise to the necessity of recording business transaction in books. They are written in a set of books in a systematic manner so as to facilitate proper study of their results.

There are three classes of accounts:

(i) Personal account,

(ii) Property accounts, and

(iii) Nominal accounts.

Management accounting provides the accounting data for taking business decisions. The accounting techniques are very essential for the success of the firm because profit maximisation is the major objective of the firm.

(vi) Managerial Economics and Mathematics:

Mathematics is yet another important subject closely related to managerial economics. For the derivation and exposition of economic analysis, we require a set of mathematical tools. Mathematics has helped in the development of economic theories and now mathematical economics has become a very important branch of the science of economics.

Mathematical approach to economic theories makes them more precise and logical. For the estimation and prediction of economic factors for decision making and forward planning, the mathematical method is veryhelpful. The important branches of mathematics generallyused by a managerial economist are geometry, algebra and calculus.

The mathemati-cal concepts used by the managerial economists are the logarithms and exponential, vectors and determinants, input-output tables. Operations research which is closely related to managerial economics is mathematical in character.

1.6 ROLE OF MANAGERIAL ECONOMICS IN BUSINESS DECISION

Decision making is an integral part of today's business management. Making a decision is one of the most difficult tasks faced by a professional manager. Amanager has to take several decisions in the management of business. The life of a manager is filled with making decisions alter decisions.

Decision making is a process and a decision is the product of such a process. Managerial decisions are based on the flow of information. Decision making is both a managerial function and an organisational process. Managerial function is exercised through decision making.

The purpose of decision making as well as planning is to direct human behaviour and effort towards a future goal or objective. It is organisational in that many decisions transcend the individual manager and become the product of groups, teams, committees, etc.

Once the decision is taken it is implemented within the minimum time and cost. A study of the principles of business decisions will enable managers to understand business problems in a better perspective and increase their ability to solve business problems facing them in the management of business.

Executives make many types of decisions connected with the business such as production, inventory, cost, marketing, pricing, investment and personnel. In the long-run, application of principles of business decisions will result in successful outcomes. Agood decision is one that is based on logic, considers all available data and possible alternatives and applies the quantitative approach.

Organisa-tional decisions are those which the executive makes in his personal capacity as a manager. They include the adoption of the strategies, the framing of objectives and the approval of plans. These decisions can be delegated to the organisational members so that decisions could be implemented with their support. These decisions aim at achieving the best interests of the organisation. The basic decisions are those which are more important, they involve long-range commitment and heavyexpenditure of funds.

Ahigh degree of importance is attached to them. Aserious mistake will endanger the company s existence. The selection of a location, selection of a product line, and decision relating to manage the business are all basic decisions. They are considered basic because they affect the whole organisation.

1.6.1 IMPORTANT TYPES OF BUSINESS DECISIONS

(i) Production Decisions:

Production is an economic activity which supplies goods and services for sale in a market to satisfyconsumer wants therebyprofit maximisation is made possible. The business executive has to make the rational allocation of available resources at his disposal. He may face problems relating to best combination of the factors to gain maximum profit or how to use different machine hours for maximum production advantage, etc.

(ii) Inventory Decision:

Inventory refers to the quantity of goods, raw material or other resources that are idle at any given point of time held by the firm. The decision to hold inventories to meet demand is quite important for a firm and in certain situation the level of inventories serves as a guide to plan production and is therefore, a strategic management variable. Large inventory of raw materials, intermediate goods and finished goods means blocking of capital.

(iii) Cost Decisions:

The competitive ability of the firm depends upon the ability to produce the commodity at the minimum cost. Hence, cost structure, reduction of cost and cost control has come to occupy important places in business decisions. In the absence of cost control, profits would come down due to increasing cost.

Business decisions about the future require the businessmen to choose among alternatives, and to do this, it is necessary to know the costs involved. Cost information about the resources is very essential for business decision making.

(iv) Marketing Decisions:

Within market planning, the marketing executive must make decisions on target market, market positioning, product development, pricing channels of distribution, physical distribution, communica-tion and promotion. A businessman has to take mainly two different but interrelated decisions in marketing.

They are the sales decision and purchase decision. Sales decision is concerned with how much to produce and sell for maximising profit. The purchase decision is concerned with the objective of acquiring these resources at the lowest possible prices so as to maximise profit. Here the executive's basic skill lies in influencing the level, timing, and composition of demand for a product, service, organisation, place, person or idea.

(v) Investment Decision:

The problems of risks and imperfect foresight are very crucial for the investment decision. In real business situation, there is seldom an investment which does not involve uncertainties. Investment decision covers issues like the decisions regarding the amount of money for capital investment, the source of financing this investment, allocation of this investment amongdifferent projects over time. These decisions are of immense significance for ensuring the growth of an enterprise on sound lines. Hence, decisions on investment are to be taken with utmost caution and care by the executive.

(vi) Personnel Decision:

An organisation requires the services of a large number of personnel. These personnel occupy various positions. Each position of the organisation has certain specific contributions to achieve organi-sational objectives. Personnel decisions cover the areas of manpower planning, recruitment, selection, training and development, performance appraisal, promotion, transfer, etc. Business executives should take personnel decisions as an essential element.

1.7 SUMMARY

Managerial economics generally refers to the integration of economic theory with business practice. Economics provides tools and managerial economics applies these tools to the management of business. In simple terms, managerial economics means the application of economic theory to the problem of management. Managerial economics may be viewed as economics applied to problem solving at the level of the firm.

It enables the business executive to assume and analyse things. Every firm tries to get satisfactory profit even though economics emphasises maximising of profit. Hence, it becomes neces-sary to redesign economic ideas to the practical world. This function is being done by 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

The usefulness of business economics lies in borrowing and adopting the toolkit from economic theory, incorporating relevant ideas from other disciplines to take better business decisions, serving as a catalytic agent in the process of decision making by different functional departments at the firm's level, and finally accomplishing a social purpose by orienting business decisions towards social obligations.