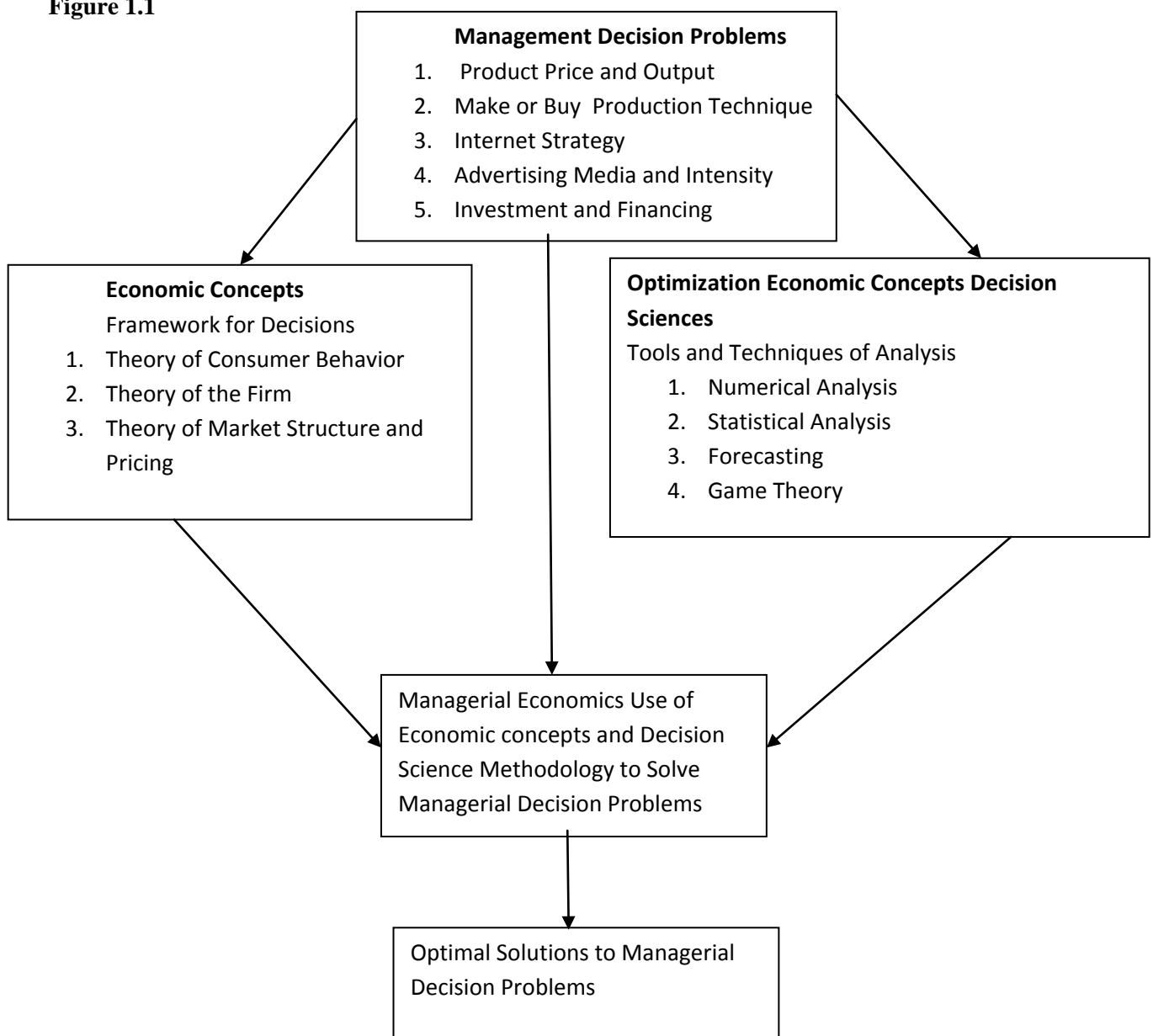


Managerial economics applies economic theory and methods to business and administrative decision making. Managerial economics prescribes rules for improving managerial decisions. Managerial economics also helps managers recognize how economic forces affect organizations and describes the economic consequences of managerial behavior. It links traditional economics with the decision sciences to develop vital tools for managerial decision making. This process is illustrated in Figure 1.1.

THE ROLE OF MANAGERIAL ECONOMICS IN MANAGERIAL DECISION MAKING
 Managerial economics uses economic concepts and decision science techniques to solve managerial problems.

Figure 1.1



Nature and Scope of Managerial Economics

Scope of Managerial Economics:

Well scope is something which tells us how far a particular subject will go. As far as Managerial Economic is concerned it is very wide in scope. It takes in to account almost all the problems and areas of manager and the firm. ME deals with Demand analysis, Forecasting, Production function, Cost analysis, Inventory Management, Advertising, Pricing System, Resource allocation etc. Following aspects are to be taken into account while knowing the scope of ME:

1. Demand analysis and forecasting:

Unless and until knowing the demand for a product how can we think of producing that product. Therefore demand analysis is something which is necessary for the production function to happen. Demand analysis helps in analyzing the various types of demand which enables the manager to arrive at reasonable estimates of demand for product of his company. Managers not only assess the current demand but he has to take into account the future demand also.

2. Production function:

Conversion of inputs into outputs is known as production function. With limited resources we have to make the alternative uses of this limited resource. Factor of production called as inputs is combined in a particular way to get the maximum output. When the price of input rises the firm is forced to work out a combination of inputs to ensure the least cost combination.

3. Cost analysis:

Cost analysis is helpful in understanding the cost of a particular product. It takes into account all the costs incurred while producing a particular product. Under cost analysis we will take into account determinants of costs, method of estimating costs, the relationship between cost and output, the forecast of the cost, profit, these terms are very vital to any firm or business.

4. Inventory Management:

What do you mean by the term inventory? Well the actual meaning of the term inventory is stock. It refers to stock of raw materials which a firm keeps. Now here the question arises how much of the inventory is ideal stock. Both the high inventory and low inventory is not good for the firm. Managerial economics will use such methods as ABC Analysis, simple simulation exercises, and some mathematical models, to minimize inventory cost. It also helps in inventory controlling.

5. Advertising:

Advertising is a promotional activity. In advertising while the copy, illustrations, etc., are the responsibility of those who get it ready for the press, the problem of cost, the methods of determining the total advertisement costs and budget, the measuring of the economic effects of advertising --- are the problems of the manager. There's a vast difference between producing a product and marketing it. It is through advertising only that the message about the product should reach the consumer before he thinks to buy it. Advertising forms the integral part of decision making and forward planning.

6. Pricing system:

Here pricing refers to the pricing of a product. As you all know that pricing system as a concept was developed by economics and it is widely used in managerial economics. Pricing is also one of the central functions of an enterprise. While pricing commodity the cost of production has to be taken into account, but a complete knowledge of the price system is quite essential to determine the price. It is also important to

understand how product has to be priced under different kinds of competition, for different markets.

Pricing = cost plus pricing and the policies of the enterprise

Now it is clear that the price system touches the several aspects of managerial economics and helps managers to take valid and profitable decisions.

7. Resource allocation:

Resources are allocated according to the needs only to achieve the level of optimization. As we all know that we have scarce resources, and unlimited needs. We have to make the alternate use of the available resources. For the allocation of the resources various advanced tools such as linear programming are used to arrive at the best course of action.