KENYATTA UNIVERSITY

UNIVERSITY EXAMINATIONS 2016/2017

FIRST SEMESTER EXAMINATION FOR THE DEGREE OF BACHELOR OF ECONOMICS

EAE 303: MANAGERIAL ECONOMICS

DATE: FRIDAY 2ND DECEMBER 2016 **TIME: 8.00 A.M. - 10.00 A.M.**

INSTRUCTIONS

1) **Answer question one and any other two questions**
2) **Question one is compulsory and carries 30 marks**
3) **All other questions carry 20 marks each**

Question One *(30 Marks)*

a) Dealing with different currencies or operating in various economies poses some threat to the firm. Exchange rate volatility can translate into heavy losses if there are adverse exchange rate changes between the date of the transaction and the date of the actual receipt or payment. Discuss three methods of foreign exchange risk management. (9 marks)

b) Describe four economies of scale that a firm is likely to experience as a result of expansion. (12 marks)

c) Macroeconomics is significant in informing managerial decisions. Giving an example of a profit maximizing firm, that produces steel for an international market; provide the rationale for integrating macroeconomics concepts in managerial economics. (9 marks)

Question Two *(20 Marks)*

a) Decision making process in any organisation follows various elements starting from identifying the objectives of the organization up to the implementation of the decision. Assume that you are the project manager of a project that you have been allocated by the county government. Discuss the various elements of decision making in light of the specific project. (10 marks)

b) The law of diminishing returns is applicable in profit making organisations in determining the amount of a variable input to employ. State the law and use an appropriate diagram(s) to illustrate and explain the profit maximizing amount of a variable input that a firm chooses to employ. (10 marks)

Question Three *(20 Marks)*

a) In a free enterprise system, economic profits play an important role in guiding the decisions made by the thousands of competing independent economic units. There are different theories that guide the expected profits from a firm. Assume that you are a manager to one of the hotels in the java franchise coffee shops in Sudan where incomes are growing and the shop is the only high end coffee shop in the area. Discuss two theories of profit that would guide in the prediction of profits for that center. You must give appropriate justification for each theory. (8 marks)

b) The total cost function for a firm in a perfectly competitive market is given by the equation: $TC = Q^3 - 24Q^2 + 600Q$

where TC = total cost in Kshs and Q is quantity.

i. Compute the cost and output level at which the firm maximise profit in the long-run? (7 marks)

ii. Use a diagram to illustrate the profit maximising price and output for the firm. (5 marks)

Question Four *(20 Marks)*

a) Distinguish between consumer clinics and market experiments methods of estimating demand in the market. Out of the two methods, justify the best method for forecasting demand for a new type of cooking oil in the market. (9 marks)

b) Define price discrimination. Explain factors that make it possible to discriminate prices for any firm. (6 marks)

c) Briefly explain two government policies against monopolies. (5 marks)

Question Five *(20 marks)*

a) Marshall is contemplating of investing in a machine that could efficiently produce Widgets. He can either choose machine X or Y. The cash flows from each machine for the various years are as shown in the table below:

Year	Machine X	Machine Y
0	(30,000)	(30,000)
1	20,000	12,000
2	18,000	16,000
3	17,000	18,000
4	15,000	15,000
5	15,000	15,000

Given the opportunity cost of capital, r, is 15% and using Net Present Value, which machine would you advice Marshall to invest in? (10 marks)

b) Assume that you are tasked with explaining to the board members of a firm in an oligopolistic market the reason why the price for the firm's product has been constant for a long time. Using appropriate diagrams use the concept of price elasticity to explain the reason for the price stickiness. (10 marks)

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