QP CODE: 21103182

B.COM DEGREE (CBCS) REGULAR / REAPPEARANCE EXAMINATIONS, DECEMBER 2021. Second Semester

Complementary Course - CO2CMT02 - PRINCIPLES OF BUSINESS DECISIONS

Instructions to Private candidates only: This question paper contains **two sections**. Answer **SECTION I** questions in the answer-book provided. **SECTION II**, Internal examination questions must be answered in the question paper itself. Follow the detailed instructions given under **SECTION II**

SECTION I Max. Marks : 80

Part A (*Answer any **ten** questions. Each question carries **2** marks).*

1. What is a decision?
   Decision is the process of deciding something or of resolving a question. Decision can be defined as a course of action consciously chosen from available alternatives for the purpose of the desired result

2. Write any two limitations of law of demand.
   - Inferior goods of giffen goods
   - Prestige goods
   - Consumer expectation
   - Consumer's misconception
3. What is meant by company demand and industry demand? Write an example.
   Company demand refers to the demand for the products of particular company. For example, the demand for cement produced by Larson & Tubro is a Company demand. Industry demand refers to the total demand for the products produced by all firms taken together in an industry. In other words, it is the sum of all company demands in an industry. The total demand for cement produced by all cement companies in India is an example of industry demand.
4. What is price elasticity of demand?
   Price elasticity of demand refers to the degree of responsiveness of consumers to a change in price of a product. Consumer's response to changes in price will be in terms of the changes in quantity demanded. In other words, price elasticity of demand is the ratio of the percentage change in quantity demanded to a percentage change in price.
5. What is cross elasticity of demand?
   Cross elasticity of demand indicates the relationship between the demand of one product with the price of another product. It may be defined as the degree of responsiveness of demand for one product in response to a change in the price of another product. Cross elasticity of demand between two substitute goods is positive.
6. What is average product?
   Average product of a particular input is the amount of output produced by that input divided by the quantity of that input used.

7. What is the role of law of diminishing returns in decision making?
   Law of Diminishing Returns or Law of Variable Proportions Law of diminishing returns examines the input output relation when the output is increased by varying one variable input. As per the law of diminishing returns if the quantity of a variable input is increased continuously, keeping the quantity of other inputs constant, the output will first increase but after a stage the output will decline.
8. Why two isoquants never intersect each other?
   Two Isoquants cannot cut each other. It means that an input combination that can produce a particular quantity of output cannot produce another quantity of output in a given state of technology. If two Isoquants, one representing 50 units of output and the other representing 60 units of output intersect each other, it means that the same input combination that can produce 50 units can also produce 60 units. This cannot happen when the technique of production remains the same.
9. What is cost function?
   It is the relationship between the price/cost of inputs and the quantity of output produced.

10 Distinguish between pure competition and perfect competition.
Pure competition is said to exist when the first three conditions such as existence of large number of buyers and sellers, identical products, free entry or exit of firms are fulfilled. Perfect competition is much broader than pure competition with additional conditions as stated earlier.

11 What is absolute monopoly?
Absolute monopoly is a situation in which there is only a single seller of product having no close substitute and there is absolutely zero level of completion. Such monopoly is practically very rare. Such monopoly is also called perfect monopoly,

12 Explain cost plus pricing
Cost plus pricing is a very common method of pricing. In this method the price of a product is fixed by adding a certain percentage to the average variable cost. The percentage added is called mark-up or margin. The mark up covers the per unit fixed cost and profit.

Part B*Answer any **six** questions.Each question carries **5** marks*

13 Explain the significance of discounting principle in business decision with an example.
The discounting principle is based on the concept of time value of money. The concept of time value of money considers that money earned in an earlier period is more valuable than the same amount of money earned in a later period. This is because money invested in an earlier period grows to more money in future. The significance of discounting principle in business decision can be made clear from the following example. Suppose a business firm invests an amount of Rs10,00,000 in a project. The project is expected to generate a profit of Rs.4,00,000 each at the end of first, second and third years. It means that the firm has to wait for 3 years to get a return of Rs.12,00,000. It appears that the firm is making a profit of Rs.2,00,000 (12,00,000-10,00,000).

14 Discuss the managerial uses of income elasticity of demand.

1. **Helps in sales forecasting** - The concept of income elasticity of demand is an important tool in the hands of business firms to forecast their future sales and plan their production accordingly. A producer having a product with positive income elasticity of demand can estimate his future sales depending upon the economic condition prevailing in the economy. If the economy is heading towards boom, he can anticipate good demand and if the economy shows symptoms of depression he can expect his sales to decline.

2. **Helps in production planning** – After forecasting the sales by making use of the concept of income elasticity of demand, a business firm can plan its production accordingly. If an increase in sales is anticipated steps should be taken to ensure smooth supply of goods as per the demand conditions. This will include ensuring availability of raw materials, working capital, labour etc.

3. **Helps in designing marketing strategies** - The knowledge of income elasticity of demand plays a significant role in designing the marketing strategies of a firm. A producer producing a product with high income elasticity of demand should focus his attention in Setting up retail outlets in those regions where income is rapidly increasing. The advertisement campaigns should also be focused in these areas.

15 Write a note on the survey techniques used for demand forecasting.

Under survey method surveys are conducted to collect data relating to future demand of a product. The data is collected either directly from the customers or from retailers, salesmen and other sales experts who are in close contact with the customers. Survey method is quite useful for short term demand forecasting of consumer goods. On the basis of the source from which data is collected they are divided into:

(a) Direct interview method - data relating to future demand of a product is directly collected from customers. It may be either complete enumeration survey or sample survey.

(b) Delphi Method - Under this method, opinions about the future demand of a product are collected separately from a panel of experts. Then each expert is told about the prediction of other experts without revealing the identity of each other. Each one is then asked to revise his prediction in the light of others opinions. The experts are again shown each other’s revised forecasts and asked to reconsider their forecasts in the context of other’s revised forecasts. This process continues till a common consensus is arrived.

16 What are internal economies of scale?

Internal economies are those economies which accrue to a single firm due to its increase in scale of operations. The source of internal economies to a large firm is from the use of more efficient production methods and efficient management of resources. According to Alfred Marshall “the chief advantage of production on a large scale are economy of skill, economy of machinery and economy of materials”. Internal economies may be of the following kinds;

- Technical Economies
- Economy of labour

- Managerial Economies
- Commercial Economies
- Economy of Capital
- Risk bearing economies

17 What are the general determinants of cost?

- Output Cost
- Prices of factors of production
- Productivities of factors of production
- Technology

18 What are the objectives of pricing?

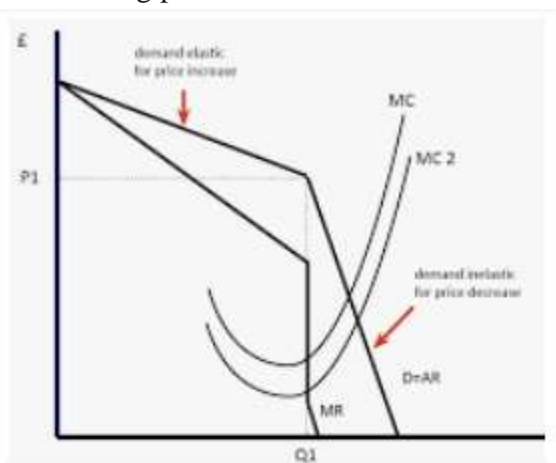
- Ensuring a target return on investment
- Market share
- Preventing competition
- Stability in price
- Profit
- Pricing based on customer's ability
- Resource mobilisation

19 What is meant by product differentiation?

Product differentiation is what makes your product or service stand out to your target audience. It's how you distinguish what you sell from what your competitors do, and it increases brand loyalty, sales, and growth. The goal of product differentiation is to create a competitive advantage or to make your product superior to alternatives on the market. Different types of product differentiations are: vertical differentiation, horizontal differentiation and mixed differentiation

20 Explain kinked demand curve theory.

A kinked demand curve occurs **when the demand curve is not a straight line but has a different elasticity for higher and lower prices**. This model of oligopoly suggests that prices are rigid and that firms will face different effects for both increasing price or decreasing price.



Kinked Demand Curve

21 Explain pricing under collusion in olig0ooly.

Firms in an oligopoly may collude to set a price or output level for a market in order to maximize industry profits. Oligopolists pursuing their individual self-interest would produce a greater quantity than a monopolist, and charge a lower price. Collusive arrangements are generally illegal. Collusion occurs when oligopoly firms make joint decisions, and act as if they were a single firm. Collusion requires an agreement, either explicit or implicit, between cooperating firms to restrict output and achieve the monopoly price. **(value liberally)**

Part C *Answer any **two** questions. Each question carries **15** marks.*

22 Define Decision making. Explain the steps involved in decision making.

According to G.R Terry, "Decision making is the selection based on some criteria from two or more possible alternatives."

Steps involved in decision making process are:

- Problem Identification
- Problem Design
- Discovering Alternatives
- Evaluating Alternatives
- Selecting the best Alternative
- Implementation
- Follow Up

23 How does analysis of demand contribute to business decision making?

In order to make decisions about the future level of production, it is necessary to analyze and estimate future demand. The analysis of demand helps in business decision making for:

- Product Planning
- Capital Investment Decision
- Advertising and Promotional expenditure decisions
- Inventory Management
- Macro economics planning
- Launching a new product

24 Explain the law of returns to scale with the help of an example

The law of returns to scale means the change in output or returns where all the factors are increased in the same ratio. In other words, in returns to scale, we analyse the effect of doubling, trebling, and so on of all the inputs on the output.

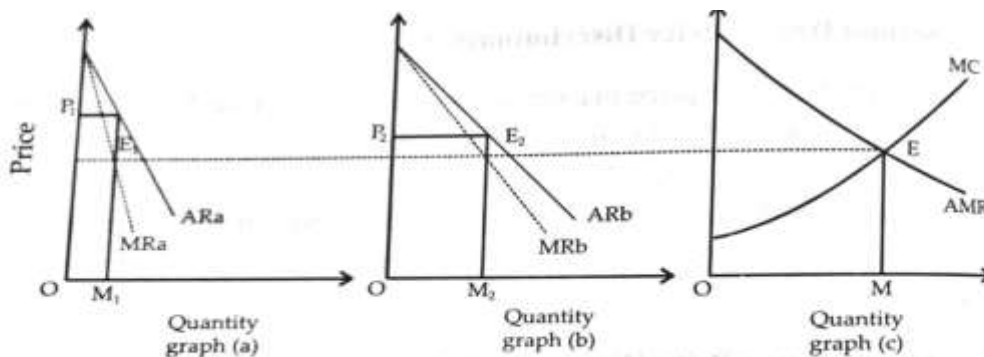
Returns to Scale

The law of returns to scale explains how a simultaneous and proportionate increase in all the inputs affects the total output. The increase in output may be proportionate, more than proportionate or less than proportionate. If the increase in output is proportionate to the increase in inputs it is **constant returns to scale**. If it is less than proportionate it is **diminishing returns to scale**. The increasing returns to scale comes in operation first, then constant and then diminishing returns to scale.

(Example required.)

25 Explain price determination under price discrimination.

A simple monopolist charges a single price for the whole output while a discriminating monopolist charges different prices in different markets Thetefore it is essential that the total market should be divided into different sub markets on the basis of price elasticity of demand in each market. The principle of MC=MR as used by a simple monopolist is used by a discriminating monopolist to determine the equilibrium price and output. To explain the process of price determination under price discrimination, we assume that the total market is divided into two sub markets A and B. Price elasticity of demand in market A is less than that of market B. Therefore a high price can be charged in market A than market B.



MR is the marginal revenue curve in sub market and corresponding to average revenue curve is AR. AMR curve represents the total amount of output that can be sold in two sub markets taken together. MC is the marginal cost curve of the total output of the product. The profit of the discriminating monopolist will be maximum at a level of output OM where MC curve intersects AMR. Therefore he will decide to produce OM level of output.

After deciding the total output the next task is to distribute the total output between sub markets A and B in such a way that MR in each market is equal to ME which is the marginal cost, being on the MC curve. Therefore he will allocate output OM1 in market A because only at this output MRa in market A is equal to ME in the total market (MIEI=ME). The price charged in market A is equal to OP1. |

Similarly OM2 level of output will be allocated in market B because only at this output MRb in market B is equal to ME in the total market. The price charged in market B is OP2 which is lower than the price in Market A. This is because of the lower elasticity of demand in Market B. OM level of the output in the total market will be equal to OM1 level of output in submarket A plus OM2 level of output in submarket B.

A discriminating monopolist will be in equilibrium if the following two conditions are fulfilled.

a) Marginal cost of total output should be equal to aggregate marginal revenue.

b) Marginal revenue in market A=Marginal revenue in market B = Marginal cost of total market

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PRINCIPLES OF BUSINESS DECISIONS

SECTION II

1. a
2. c
3. c
4. b
5. c
6. c
7. b
8. d
9. a
10. d
11. b
12. c
13. a
14. b
15. d
16. b
17. b
18. b
19. c
20. c