Roll No. ____________________

(Do not write anything on question paper except Roll No.)
[This paper consists of FOUR Pages]

Jagan Institute of Management Studies
End-Term Examination, September, 2016
Trimester I – PGDM (IB)/PGDM (RM) 2016-18

Managerial Economics
ET_IB_RM_ME_2909

Time: 3 Hrs. *M. Marks: 70*

INSTRUCTIONS: Attempt any FIVE questions including Q1 & Q7 which are compulsory.

Q 1 Attempt any **SIX** of the following:

a) Being a manager in an FMCG firm, elucidate how the concept of scarcity and opportunity cost would affect your decision making.

b) In 2006, the management of the Indira Gandhi International Airport at New Delhi was handed over to DIAL, a consortium of the GMR Group. The airport was rated as the *Best airport in the world* in the 25–40 million passengers category in 2015, by Airports Council International. Apart from the private costs that DIAL incurred in upgrading the airport, discuss some social costs to the society from the airport.

c) There is generally scope for bargaining by the customer at a roadside vegetable vendor as against an organized store like Big Bazaar. In view of this statement, discuss the difference in price elasticity of vegetables from a vendor as against a departmental store.

d) Discuss the difference in values obtained while calculating economic profits and accounting profits.

e) Identify some barriers to entry in the housing infrastructure industry.

f) The computed income elasticity of demand for home water heaters is +0.15. Can you think of products/ cases when income elasticity is negative in nature?

g) Explain how Giffen goods are an exception to the Law of Demand.

h) Discuss the process of price determination in an economy following the invisible-hand mechanism. **18**

Q 2 How will the area manager of a courier company utilize the various managerial economics concepts in order to take routine and strategic decisions to achieve organizational success? **12**

Q 3 a) A drive-in theatre is a form of cinema structure consisting of a large outdoor movie screen, a projection booth, a concession stand for snacks and assorted accessories and a large parking area for automobiles. Within this enclosed area, customers can view movies from the privacy

and comfort of their cars. Some drive-ins have small playgrounds for children and a few picnic tables or benches.
How would the demand curve of the conventional theatre (cinema hall) change if drive-in theatres were introduced and promoted in the Indian cities? Show this change diagrammatically, giving due reasons for the same. **6**

b) Illustrate the difference between the marginal and the incremental principal of maximizing profit. **6**

Q 4 a) Why the Law of Variable Proportions is generally observed in the farming sector as against the more organized manufacturing sector? **8**

b) At which stage is a rational producer more likely to produce and why? **4**

Q 5 a) Why the long run average cost curve (LRAC) is called the 'planning curve'? **6**

b) Why is the seller in a perfectly competitive industry known as the 'price taker' and not a 'price maker'? **6**

Q 6 a) How is the Delphi method used to forecast future demand? **6**

b) Why prices tend to be sticky in oligopolistic markets? **6**

Q 7 Read the article and answer the questions that follow.
This is a story of a small retailer in Arkansas that started in 1945. The company went public in 1970 with thirty stores located in Arkansas, Missouri, and Oklahoma (The United States). In 1985 the company had 859 stores in 22 states of the US. By 2010 the company had over $400 billion in revenue, operated over 3,000 stores in every state, and employed 2.1 million people. This is the story of Wal-Mart.

So how did Wal-Mart grow from a single branch in Arkansas to the largest retailer in the world? Wal-Mart is one of the most unbelievable growth stories ever. Yet, it accomplished this feat in the most competitive market with no patents, government licenses, or massive amounts of R&D.

There are many myths about how Wal-Mart achieved its growth. Some of these myths include; putting pressure on vendors, having a monopoly in small towns, better management, and that products are cheaper in the southern states. Instead of focusing on the myths, let us focus on the facts of how Wal-Mart truly achieved its dominance.

The best time period to evaluate the mega store is the mid-1980s. This is when Wal-Mart was at its peak, and Kmart (a competitor) was declining. In 1985, Wal-Mart had far higher operating margins, and returns on capital than Kmart. So what made Wal-Mart excel, while

Kmart falter? The answer lies in declining costs while expanding size and scope.

In 1985 despite operating nearly 1,000 stores, 80% of Wal-Mart's stores were located in Arkansas, and adjacent states. By contrast Kmart was much more spread out, despite having its own area of concentration in the Midwest. This helped Wal-Mart spend less money on bringing goods to its warehouses, and distributing the goods to distribution centres. Wal-Mart used its own trucks to transport merchandise, and since the distance between the distribution centres were close, Wal-Mart's costs were lower.

Wal-Mart used many local factors to its advantage to get more bang for its buck. As an industry expert states, "a thirty-second (advertisement) spot in Nashville charges the same whether there are three Wal-Mart stores in the area or thirty". This would apply whether the ad was on TV, in the newspaper, or in a circular. When Wal-Mart advertised it was able to reach a larger number of potential customers, despite paying the same price as competitors would.

The final advantage Wal-Mart had was due to the structure of its management. Executives, and store Managers would pay close attention to the local branches under their supervision. Since the stores were close, traveling time was decreased, and managers could spend more time effectively managing their stores. This territorial advantage allowed Wal-Mart to hire fewer managers. To supervise the same number of stores, a Kmart executive would have to cover territory four times as large. It is estimated that this expense may have cost Kmart 2% in additional expenses. This extra 2% is a massive difference when operating margins only hovered around 6%.

All the advantages Wal-Mart enjoyed were due to local economies of scale. Even though Kmart's revenues were three times the size of Wal-Mart's revenues in 1985, Wal-Mart was able to operate much more efficiently.

After 1985, Wal-Mart's operating margins, and return on capital started to decline. This is not surprising as Wal-Mart had nowhere else locally to expand. Wal-Mart started to open chains in California where it competed with Target. Wal-Mart also expanded to the Midwest facing competition from Kmart, and Northeast where it faced Caldor. Wal-Mart no longer had a monopoly as it did in the areas surrounding Arkansas.

What does the future hold for Wal-Mart? It does not look promising. Wal-Mart no longer has the advantages of local economies of scale. Furthermore, Wal-Mart is trying to expand overseas where it definitely does not have this advantage. Wal-Mart's expansion into places like Germany has been largely unsuccessful. If one considers the

industry experts' view, the best option for the company would be expansion into Canada, and Mexico, however Wal-Mart will likely never have the returns that it used to have.

Questions:

a) In which market structure would you classify the organized retail industry in the Indian context? Give suitable examples and justifications for your answer. **4**

b) Identify the various economies that Wal-Mart has been employing since it started operations. **4**

c) Why do you think Walmart is not able to replicate its success overseas? **4**

d) What could be the possible barriers to entry that a new player could face in this industry? **4**

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