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**GARISSA UNIVERSITY**

**UNIVERSITY EXAMINATION 2017/2018 ACADEMIC YEAR ONE**

**THIRD SEMESTER EXAMINATION**

**SCHOOL OF BUSINESS AND ECONOMICS**

**FOR THE DEGREE OF MASTER OF BUSINESS ADMINISTRATION**

**COURSE CODE: MBA 813**

**COURSE TITLE: MANAGERIAL ECONOMICS**

**EXAMINATION DURATION: 2 HOURS**

**DATE: 06/08/18 TIME: 09.00-12.00 PM**

**INSTRUCTION TO CANDIDATES**

* **The examination has FIVE (5) questions**
* **Question ONE (1) is COMPULSORY**
* **Choose any other THREE (2) questions from the remaining FOUR (4) questions**
* **Use sketch diagrams to illustrate your answer whenever necessary**
* **Do not carry mobile phones or any other written materials in examination room**
* **Do not write on this paper**

**This paper consists of THREE (3) printed pages *please turn over***

**QUESTION ONE (COMPULSORY)**

1. You have been appointed a manager of a budding shoe factory. Your position demands that you make wise and viable short-term decisions in order to steer the firm to great heights of growth. Explain the very decisions you will make **[5 marks]**
2. In an attempt to increase revenues and profits, a firm is considering a five percent increase in the price of its goods and 15 percent increase in advertising expenditure. If the price elasticity of demand is -1.5 and advertising elasticity of demand is +0.6, would you predict an increase or decrease in revenues? Explain **[5 marks]**
3. What do you understand by demand forecasting? If you are a manager of a meat factory what are the five ways that you will use to forecast demand for meat in Garissa county **[5 marks]**

**QUESTION TWO**

1. Explain the properties of indifference  **[4 marks]**
2. The principle of diminishing marginal rate of substitution demonstrates that as a consumer looses a given amount of good Y while gaining good X, the marginal rate of substitution goes on reducing. As a demonstration of this very principle, draw a clearly labeled hypothetical indifference curve and show that the slope of the tangent GH=OG/OH, the slope of the tangent KL=OK/OL and finally the slope of the tangent MN=OM/ON. If point P is at the top most of the indifference curve, while point R is at the middle of the indifference curve and S at the lowest part of the curve, what are the marginal rates of substitution of these points? What can you say about the relative sizes and magnitudes of KL, GH and MN? What does this tell us about the principle of diminishing marginal rate of substitution on an indifference curve? Explain concisely **[11 marks]**

**QUESTION THREE**

A consumer has an income of Ksh 200 rice and wheat. Assuming that the consumer’s income increases from Ksh 200 to Ksh 300, draw a well labeled consumer’s equilibrium curve explaining consumer’s consumption. Where will consumer’s equilibrium be attained and why. Show that at the equilibrium point you obtained, the slope of the budget line is equal to the marginal rate of substitution of the indifference curve to which it (the budget line) is tangent **[15 marks]**

**QUESTION FOUR**

The manager of Kawality ice cream is to decide between two investment projects. Project A is the investment in the introduction of bottles of cold milk while project B will deal with the manufacture of ice cubes. The two investment projects yield the following net cash flows and the initial expenditure.

Net cash flows

|  |
| --- |
| Investment projects Year1 Year2 Year3 initial investment |
| A 50000 70000 40000 120000 |
| B 40000 80000 50000 110000 |

1. Calculate the net present value (NPV) of each project with risk free discount rate of 8 percent **[7.5 marks]**
2. Which of the investment projects the manager should choose if the risk premium is 4 percent on project A and 9 percent on project B **[7.5 marks]**

**QUESTION FIVE**

1. By the use of a curve, show how a firm in a perfectly competitive market incurs losses. **[7.5 marks]**
2. For a perfectly competitive firm, the following short run function is given; TC=2+4Q+Q2. If the price of the product prevailing in the market is Ksh 8, at what level of output the firm will maximize profits **[7.5 marks]**