工商管理精要系列·影印版

管理经济学

Business Economics

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《工商管理精要系列·影印版》

出 版 说 明

《工商管理精要系列·影印版》是中国人民大学出版社和西蒙与舒斯特国际出版公司继《工商管理经典译丛》之后，共同合作出版的一套大型工商管理精品影印丛书。

本丛书由欧洲著名管理学院和管理咨询公司的教授和专家撰写，它将90年代以来国际上工商管理各专业的最新研究成果，分门别类加以精练浓缩，由享誉世界的最大教育图书出版商Prentice Hall出版公司出版。每一本书都给出了该专业学生应掌握的理论框架和知识信息，并对该专业的核心问题和关键理论作了全面而精当的阐述。本丛书虽然篇幅不长，但内容充实，信息量大，语言精练，易于操作且系统性强。因此，自90年代初陆续出版以来，受到欧洲、北美及世界各地管理教育界和工商企业界读者的普遍欢迎，累计发行量已达数百万册，是当今国际工商管理方面最优秀的精品图书之一。

这套影印版的出版发行，旨在推动我国工商管理教育和MBA事业的发展，为广大师生和工商企业界读者，提供一套原汁原味反映国外管理科学研究成果的浓缩精品图书。有助于读者尽快提高专业外语水平，扩大知识面，掌握工商管理各专业的核心理论和管理技巧。

本丛书可作为管理院校的专业外语教材和各类企业的培训教材，对于那些接受短期培训的企业管理者、MBA学生，以及想迅

速了解工商管理各专业核心领域的师生来说，本丛书更是极具价值的藏书和参考资料。

为了能及时反映国际上工商管理的研究成果，中国人民大学出版社今后将与 Prentice Hall 出版公司同步出版本丛书的其他最新内容并更新版本，使中国读者能借助本丛书，跟踪了解国际管理科学发展的最新动态。

1997 年 8 月

Preface

This book is not intended to create economists. Managers are not economists, nor need they be. Instead, it is intended to introduce managers and trainee managers to the essence of business economics; to those concepts, theories and ideas which form the economist's tool kit. The rationale for the book lies in a belief that, armed with an understanding of business economics, managers can understand and hence better react to changes in the competitive environment in which their businesses operate. Since business economics is a compulsory element of many professional management training courses, the book will be particularly useful for those studying on Master of Business Administration (MBA) and Diploma in Management (DMS) programmes as well as practising managers attending continuing studies courses in which business economics is an integral part. In addition, the book is also suitably structured for students attending business studies and general economics courses at universities, polytechnics and colleges of further and higher education.

In particular, the book studies the nature of consumer demand and costs of production within different types of competitive markets. Factors impacting on demand are considered and methods for forecasting demand are investigated, while the behaviour of costs over time and as output changes is studied in detail. The book contains a review of the various business objectives management might pursue and their differing implications for optimal pricing and investment policies. It also surveys the impact of government on the environment in which the firm ultimately thrives or dies and discusses in particular the nature of industrial, competition and regional policies. There is a brief introduction to macroeconomic policy and more specifically demand management, though readers requiring a more detailed treatment of this subject are directed to our companion volume in this series, *The Essence of the Economy.*

We are once again indebted to Christine Williams who has stoically dealt with the typing and retyping of the various and often almost illegible drafts of this book. We would like to acknowledge the patience and encouragement of Cathy Peck of Prentice Hall; it is no easy task to manage two independently minded authors who always promise completion of a manuscript 'tomorrow'! Our thanks also go to our MBA students at the Cranfield School of Management. They have helped to create a uniquely challenging environment for us as lecturers and authors and we owe a great deal to them. Their constant questioning has proved invaluable in focusing our ideas. We would also like to acknowledge the support of our colleagues and notably our friend Dr Frank Fishwick. Frank has that rare quality of posing the questions that no one else appears to have thought about!

Lastly, of course, the greatest tribute must be to our wives and children who have once again borne the sacrifice to family life, which results from writing, with their usual cheerfulness.

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The essence of business economics: an overview

The essence of business economics

Today, the economic, political and social environments are changing faster than ever before. Business success depends, therefore, on managers anticipating and coping with change. To do this managers must first identify the characteristics of the world in which they operate. That 'world' may be examined at the following two levels:

- **The microeconomic environment.**
- **The macroeconomic environment.**

The microeconomic environment deals with the operation of the firm in its immediate market, involving the determination of prices, revenues, costs, employment levels and so on. In contrast, the macroeconomic environment comprises the general social and economic conditions of the larger system of which each firm forms a part. This larger system involves the impact of political, legal and economic decisions, both nationally and internationally. By definition, since any single firm usually represents a minute part of the larger system, it is unlikely to be able to exercise control over the macroeconomic environment in the way in which it may be able to have control over its microeconomic environment (as in the case of a monopoly firm, for example).

The macroeconomic environment is covered in our companion volume to this series entitled *The Essence of the Economy*. In terms of Figure 1.1, this book dealt with the impact of the wider international and domestic economies on the firm; whereas the current book is solely concerned with a study of the immediate environment of the firm, i.e. business economics.

Our aim here is to meet the needs of the manager in the daily process of decision-making. Decisions, if they are to be effective, must be soundly based on a critical awareness of the fundamental economic relationships which underlie all business operations. The manager must be able to apply this understanding and knowledge to real-world problems. An understanding of the key concepts of business economics provides a sound foundation for optimal decision-making. The subjects of marketing, strategic management, finance and so on, utilize many of the core concepts introduced here.

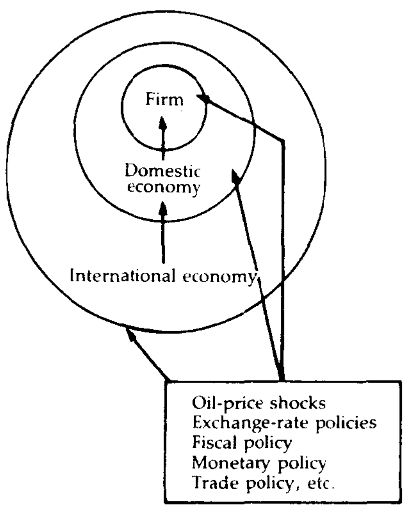

Figure 1.1 The business environment

Basic concepts in business economics

There are a number of basic concepts which lie at the heart of business economics and managerial decision-making. The most important of these are the following:

- Resource allocation.
- Opportunity cost.
- Diminishing marginal returns.
- Marginal analysis.
- Business objectives.
- Time dimension.
- Externalities.
- Discounting.

We start by briefly describing the relevance of each of these to business economics.

Resource allocation

When purchasing raw materials, employing labour and undertaking investment, the manager is involved in *resource allocation*. Society's resources are, inevitably, scarce so that the individual firm has to pay for them. Decisions need to be made at three levels, namely:

- **what** goods and services to produce with the available resources;
- **how** to combine the available resources to produce different types of goods and services, and
- **for whom** the different goods and services are to be supplied.

Figure 1.2 illustrates the interrelationship between the production decision and decisions regarding these three factors. Such decisions are sometimes described as the *allocative, productive* and *distributive* choices respectively which face society in general. In business economics we examine how the price mechanism relates to making these choices.

Traditionally, the price mechanism has been seen as the major determinant of the *what, how* and *for whom* decisions, especially in

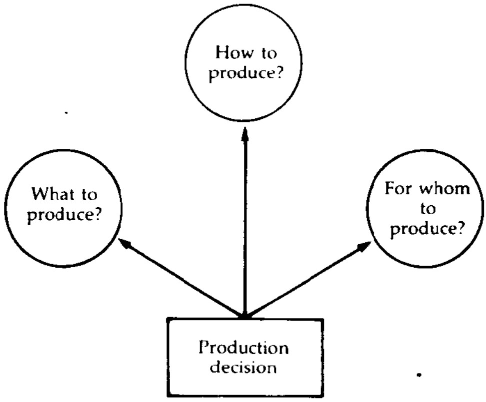

Figure 1.2 The production decision

market economies, though less so in the formerly centrally planned or command economies of Eastern Europe. However, over time in all economies firms have grown in size and importance – witness for example resource allocation which goes on *within* companies such as IBM, ICI and Toyota. Resources within firms are allocated by both command and price. For example, a decision on where to locate plant could be based upon detailed costings of alternative sites (price). Alternatively, the decision might be made by management on the basis of non-price factors, which may in fact be purely subjective ('a nice area of the country to live').

In so far as resource allocation in firms results from command rather than price, as Professor Robertson observed, firms might be considered to be 'islands of conscious power in . . . [an] ocean of unconscious co-operation' (Robertson and Dennison, 1960). The market therefore represents a network of unconscious co-operation between a multitude of buyers and sellers. At the same time, the boundary between the firm and the market is constantly evolving through mergers, takeovers, divestment, management buyouts, etc. Firms are constantly reassessing their structures and strategies and attempting to answer questions such as whether or not they should undertake in-house those activities which are currently purchased in the market (e.g. take over a supplier?), or, instead, should certain activities which are currently undertaken and purchased in the market (e.g. software development in the case of a computer manufacturer) be closed down or sold off?

The so-called 'make or buy' decision needs to be constantly monitored. The American economist Oliver Williamson has referred to this as a decision about the *boundary of the firm*. Where is the boundary of the firm to be drawn? In other words, what activities should be directed by the 'conscious power' of management and what should be the prerogative of the 'unconscious co-operation' which is the hallmark of the market? The firm or the market is a choice between the allocation of resources in 'markets' or 'hierarchies'. Sometimes it will pay to buy in the market while sometimes it will be more efficient to undertake an activity in-house. In economic terms, the deciding factor will be relative costs. The manager, therefore, needs to be aware of not only the current costs of production but also the costs of the alternative method of supply. This brings us to the economist's concept of *opportunity cost*.

Opportunity cost

Underlying business decisions is the fact that resources are scarce. This scarcity can be reflected in many ways, such as shortages of capital, physical and human resources, and time. The existence of scarcity means that whenever a decision or choice is made, a cost is incurred. Economists take a broader view of such a cost than that based purely on monetary factors as used by accountants. In economists' jargon, such costs include opportunity costs.

> **The opportunity cost of any activity is the loss of the opportunity to pursue the most attractive alternative given the same time and resources.**

The concept of opportunity cost can be usefully illustrated using a simple diagram. In Figure 1.3, the curve PP represents what is called a *production possibility curve* (PPC).

> **A production possibility curve shows the maximum output of two goods or services that can be produced given the current level of resources available and assuming maximum efficiency in production.**

Any firm with its available *factors of production* (which may be broadly categorized as land, labour and capital) has a choice as to the products it may produce. For example, suppose that a business school runs both an MBA programme and continuing studies courses for practising managers. It is able to provide either 0A places for MBA students or 0B places for practising managers or some combination of both shown along the PP curve. Now suppose that

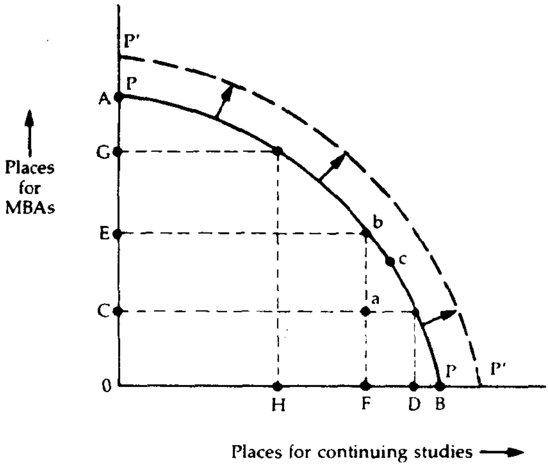

Figure 1.3 Production possibility curve

currently the business school provides 0C MBA places and 0D continuing studies places, but decides to expand its MBA provision to 0E. Given current resources, these extra MBA places can only be achieved by reducing the continuing studies activities to 0F. In other words, the opportunity cost of accommodating CE extra MBA students is DF fewer continuing studies places. Similar trade-offs between the two activities are shown along the PP curve. The *shape* of the curve reflects the fact that in business, as resources are transferred from one activity to another, the resulting increase in activity (in this case MBA places) is likely to decline. This relates to the concept of *diminishing marginal returns*.

Diminishing marginal returns

The concept of diminishing marginal returns refers to the situation whereby as we apply more of one input (e.g. labour) to another input (e.g. capital or land), then after some point the resulting increase in output becomes smaller and smaller.

For example, in the case of the business school, the transfer of equal amounts of resources from continuing studies courses to MBA provision may produce an increasingly smaller addition to the MBA output if MBA teaching requires higher-level skills than continuing studies teaching. If the business school continues to increase its MBA numbers by a given amount, it is likely to have to reduce its continuing studies places by a proportionately greater amount. For example, returning to Figure 1.3, an increase in the number of MBA students of EG (where EG = CE) leads to a fall in continuing studies places of FH. As will be appreciated from the diagram, FH is greater than DF.

Of course, if the business school had *not* been using its resources to maximum efficiency then it could have increased the number of MBA students without cutting its continuing studies courses by simply becoming more efficient (in Figure 1.3 this is shown by moving from point a, below the PP curve, to point b on the curve). Equally, it could have increased provision of *both* courses by moving to, for example, point c. To increase provision beyond the PP curve (as shown by P′P′) naturally requires more resources, e.g. lecture rooms, lecturers, etc. These sorts of choices and hence the issue of resource allocation lie at the heart of business decision-making.

Marginal analysis

The idea of opportunity cost highlights that choices have to be made regarding what to produce. The concept of *the margin* reminds us that most of these choices involve relatively small (incremental) increases or decreases in production. For example, decisions have to be made regarding whether to provide an extra MBA class, an extra production shift, to generate an extra megawatt of electricity, to produce 1,000 fewer ball-bearings, to add a product to the product range, etc. Only relatively rarely do we make decisions about all or nothing, e.g. whether to be a manufacturer or not! The scale of the increase or decrease in production – the extent of the 'marginal' change – will, of course, be related to the scale of the overall operation. For example, electricity generating companies are most unlikely to be concerned with decisions about whether or not to produce one more watt of electricity!

The concept of the margin is central to most economic decisions and hence is referred to throughout this book, both in terms of consumer behaviour when buying products and the behaviour of firms when deciding whether to alter production. Consumers, through their purchasing decisions, must decide whether or not buying a particular product will add more to their well-being than spending the same amount on some alternative. Similarly, at the heart of managerial decision-making is the question of whether or not the increase in output will provide enough extra revenue to compensate for the extra cost of production. The aim of the manager (i.e. the decision-maker in this case) is to find the optimal level of production.

Business objectives

Traditionally, the study of managerial decision-making has focused on the single objective of profit maximization. This stems from the fact that owners of businesses were considered to be simply interested in making profit. Today, no doubt many businesses are still run with an eye to maximizing profits. However, the development of modern capitalism has led to a divorce of ownership and control in modern companies. Especially in the large companies which dominate production in advanced economies, a 'managerial class' controls the company's operations, while ownership of the company is spread amongst a multitude of shareholders. This development has led to a reassessment of the view that the pursuit of maximum profit is always the firm's primary objective, even in the longer term.

In reality, management in large companies may pursue a wide range of objectives, which may not always be wholly consistent (e.g. maximizing output as against minimizing environmental damage). Profit maximization for shareholders, suitably defined, may be but one element amongst such objectives and may not be of most immediate importance in the eyes of management. Other possible objectives of managers could include the following:

- The achievement of personal goals, involving personal security and reward, status, degree of discretionary power, etc.
- Growth targets for the company in terms of scale of output, market share, geographical market, annual extension of physical capacity, size of departments or size of the labour force, etc.
- Maximization of sales revenue (as opposed to sales volume).

It is possible, of course, that managers at any given time may not be actively attempting to maximize any particular goal, preferring instead to achieve a *satisfactory* level of performance across a range of indicators, including the attainment of simply an adequate level of profits to satisfy shareholders' expectations and thereby retain their confidence (and their own jobs!).

Ascertaining the objective(s) of management is, of course, important as the objective pursued determines actions taken such as, for