**MBA 540 Mid-term Exam**

1. (10 pts.) Stella Ann Freeman is having a difficult time deciding whether or not to purchase a new car. How would understanding the concept of opportunity costs help her make a decision?

2. (10 pts.) Referring to the table below, hiring a driver costs $10. Each machine costs $100. Which method should he use and why?



3. (10 pts.) Enron will be an example of a dysfunctional company for many years to come. It was clearly a company riddled with fraud and excess and its conduct drove it into bankruptcy. The text argues that individual behavior was not at the core of Enron’s problems. What were the problems with this corporation from an organizational architecture point of view?

4. (10 pts.) For many corporations such as utility companies, a major portion of the cost of production is fixed in the short run. Should these very large fixed costs be ignored when the executives are making output and pricing decisions? Why?

5. (10pts.) Choose a real-life example of a firm that you think is part of an oligopoly market and describe the characteristics of the market structure that explain why the firm would be classified as such.

6. (10 pts.; 2 pts each) You are the manager for Dunkin Donuts and know the following elasticities:

 η= 1.5 η I = 1.2 η xy1 = 0.5 η xy2 = -0.5

η is the price elasticity of demand for Dunkin Donuts (DD) glazed doughnuts, ηxy1 is the cross elasticity of demand between DD glazed doughnuts and Krispy Kreme (KK) glazed doughnuts, ηxy2 is the cross elasticity of demand between DD glazed doughnuts and DD French Vanilla coffee, and η I is the income elasticity of DD glazed doughnuts.

1. If you want to increase your sales of glazed doughnuts by 30%, in what direction and by how much do you need to change the price?
2. If you make the percentage price change that you calculated in part a) will total revenue increase or decrease? How do you know?
3. Krispy Kreme lowers its price of glazed doughnuts by 20%. The demand for Dunkin Donuts glazed doughnuts will change by what percentage and in what direction?
4. Dunkin Donuts raises the price of its French Vanilla coffee by 15%. The demand for Dunkin Donuts glazed doughnuts will change by what percentage and in what direction?
5. If average income increases by 5% by what percentage and in what direction will the demand for Dunkin Donuts glazed doughnuts change? Are DD glazed doughnuts a normal good or an inferior good and how do you know?

7. (10 pts.) Westinghouse and General Electric are competing on the newest version of clothes washer and dryer combinations. Two pricing strategies exist: price high or price low. The profit from each of the four possible combinations of decisions is given in the following payoff matrix:

|  |  |  |
| --- | --- | --- |
|  |  |  *Westinghouse’s price* |
|  |  | *High ($4000)* | *Low ($2000)* |
| **General Electric’s****price** | **High ($4000)** | *W: $10,000,000***GE: $10,000,000** | *W: $16,000,000***GE: $-4,000,000** |
| **Low ($2000)** | *W: $-4,000,000***GE: $16,000,000** | *W: $4,000,000***GE: $4,000,000** |
|  |  | Payoffs in dollars of profit. |

a) (2 pts.) Which strategy offers both Westinghouse and General Electric the best financial outcome?

b) (2 pts.) Does either firm have a dominant strategy? If yes, which firm and what strategy?

c) (4 pts.) The Nash equilibrium is for Westinghouse to set its price at \_\_\_\_\_\_\_\_\_\_ and earn a profit of \_\_\_\_\_\_\_\_\_\_ and for General Electric to set its price at \_\_\_\_\_\_\_\_\_\_\_\_\_\_ and earn a profit of \_\_\_\_\_\_\_\_\_\_\_\_\_.

d) (2 pts.) Why do we see that the strategy that results is not the strategy that offers both players the best financial outcome?