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Understanding the Link Between Managerial Economics, Business Strategies Formulation and Implications

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Abstract

Managerial economics as a field of study has become popular in recent times as a result of the increasing variability of business environments. Business organizations' demand for tools that will aid them in making informed decisions in an environment characterized by change and competition has become increasingly prevalent. This study theoretically examines the relationship between managerial economics and business strategies formulation and identified eight different strategy methods that form the basis for smart decision-making processes for managers who aim to increase their profitability, market share and competitiveness. In establishing the link between these two concepts – both which are essential for a company to grow, thrive and compete in an environment of uncertainties in the business world, the study identified the critical elements managers need for achieving its goals and optimizing its financial success. Practically, this study would expose top managers on how to strategically plan organizational programs no matter how small because no organizational program is insignificant.

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Introduction
Managerial Economics is a relatively new science. The rising erraticism and unpredictability of the business environment in Nigeria and globally has caused business managers to become increasingly anxious about finding logical ways of adjusting to an unfavourable business environment (Chand, 2016). Business managers and owners in all sectors face an extensive range of challenges. All businesses involve dealing with people, whether individuals or corporations and except in ideal situations, people are largely known to be unpredictable and sometimes irrational. There are three types of uncertainty that plague businesses (Lander, 2017); First, State uncertainty which refers to when a manager is unable to determine what could happen as a result of the business environment. For example, a food vendor at a university in Nigeria faces state uncertainty due to the threat of strike which could occur at any time. Second, Effect Uncertainty occurs after the state uncertainty. After a business owner has determined what could happen, he faces effect uncertainty. It refers to when a manager can't figure out how the events might affect his business either now or in the future. The food vendor at University of Port-Harcourt who knows a strike will happen could be uncertain about whether students will choose to go home or remain in their accommodation while the strike is on-going. And third ,Response Uncertainty occurs after effect uncertainty. Response uncertainty refers to a manager's inability to be sure of how the market will react to the actions taken. The food vendor who has found out that 50% of students have gone home may be uncertain about whether the available students' demand will be sufficient for him to cover costs and make profits.

The different levels of uncertainties stated above indicate that business environment is largely unpredictable and full of challenges. These uncertainties fall within demand, market and transactional regimes. The demand and transactional uncertainties occurbecause businesses cannot completely determine the movement of demand and outcome of a transaction in regard to the movement of other variables like price, promotion, business policies and product development. Further, the market uncertainties arise when businesses cannot completely determine the behavior asserted by the market or customers over a specific time frame. Hence, business organizations are always looking out for ways and means to influence their dealings with these uncertainties. Supportively, Chand (2016) stated that managerial economics as an idea was popularized in recent times as a result of the increasing variability of business environments. The author opined that business problems brought about increased attention of academia on managerial economics since 1950. Same study noted that it was first made popular in USA by Joel Dean in a publication titled "Managerial Economics" in 1951.

The need for managerial economics is traceable to the needs of businesses in acquiring tools and techniques as an aid to formulate strategies, evaluate and implement them. Similarly, David (2011) noted that formulation of strategies' decision ties an organization to adoption of specific resources, products, technologies and market over a long period of time. Nwachukwu, Chlandkova, Fadeyi (2017) observed that strategies formulation involves matching firms' internal resource with what the external environment provides. Additionally, Katsvamutima and Jeevananda (2014) studied the relationship between strategy formulation and implementation of food firms in Zimbabwe. The study found out that formulation of strategy and implementation enhances profitability and competitiveness of businesses. However, using the right managerial tool becomes an essential aspect of business organizational management. Insofar, most studies that have looked at the subject matter have not deemed it

necessary to blend managerial economics and business strategies formulation. Hence this study focuses on linking the relationship between managerial economics and business strategies formulation and its implication for making informed business decisions. In examining the subject of understanding the link between managerial economics, business strategies formulation and implications, this study shall x-ray the following important concepts like; The business decisions made by leaders under a limited amount of resources and how these affect business strategies formulation and implementation. How business uncertainties affect managerial decisions, strategies formulation and implementation. Through the understanding of managerial economics, a business leader can easily forecast the future and design programs that will successfully ameliorate the unforeseen uncertainties. If practical application of managerial economics theories will help in solving business and management problems. If there is a relationship between managerial economics, business strategies formulation and implication by focusing on decision-making process, decision models and decision variables.

The Objective of This Study

The objective of this study is to establish a relationship between managerial economics, business strategies formulation and implication. The study will provide explanations for the following business activities that are critical to the survival of every enterprise.

a. The adequacy of the application of economic principles and methodologies to the decision-making process within the firm or organization under the condition of uncertainty.

b. The benefits derivable from using managerial economics theories to solving business challenges on daily basis.

c. The identification of valuable business strategy resources that aids a firm to achieve sustainable competitive advantage and higher profitable returns.

d. State business strategy tools that will enhance the performance of internal resources such as assets, capabilities, firm attributes, information and organizational processes that will create economic value to businesses through effective decision making.

e. Identify the functional business areas where managerial economics principles will assist in providing solutions to solving management problems.

Theoretical Framework

Mansfield, (2015) defines managerial economics as the “application of economic principles and methodologies to the decision process within the organization. It seeks to establish rules and principles to facilitate the attainment of the desired economic goals of management.” Joel Dean, one of the fathers of the field proposes that "the purpose of managerial economics is to show how economic analysis can be used in formulating business policies". Lastly, Professor Evan J. Douglas states “Managerial economics is concerned with the application of economic principles and methodologies to the decision-making process within the firm or organization under the conditions of uncertainty” (Managerial Economics Club, 2016). The common thread in all these definitions is that managerial economics is integral for making informed decisions in business especially given the risk of uncertainty. Anandi P Sahu, (2007)has provided insight into some examples of managerial decisions business managers and organisations are confronted with on daily basis. These managerial decisions are: First, Deciding the price of a product and the quantity of the commodity to be produced. Second, Deciding whether to manufacture a product or to buy from another manufacturer. Third, Choosing the production technique to be employed in the production of a given product. Fourth, Deciding on the level of inventory a firm will maintain of a product or raw material. Fifth, Deciding on the

advertising media and the intensity of the advertising campaign. Last, Making employment and training decisions & Making decisions regarding further business investment and the mode of financing the investment.

Managerial economics is a blend of microeconomics, macroeconomics and management. Microeconomics is the study of the behaviour of individual consumers and firms while Macroeconomics is the study of the economy as a whole. While both micro and macroeconomics are essential, microeconomics forms the foundation of managerial economics. The major principles of microeconomics that form the core of Managerial economics are Demand Analysis and Forecasting, Theory of Price, Theory of Revenue and Cost, Theory of Supply and Production. This is what business entails and it is about making the right decisions; all managers and business owners want to make decisions that maximise their efficiency and profit (Juneja, 2018). Managerial economics involves the use of economic concepts, theories, apparatus, and methodologies to resolve real life business problems; it aids managers in making decision and serves as a bridge between practice and theory (Allen, 2012). Managerial economics is a branch of Economics uses microeconomic analytical methods in business decisions; it is most times referred to as business economics (Trivedi, 2002). Also, Chand (2019) stated that managerial economics is an integration of economic theory with business activities and practices. Wilkinson (2005) identified several areas that managerial economics relates with. They include economic theory, decision science and business functions. The economic theory deals with market and interaction with various elements of the micro aspect of an economy. Such as: Theory of the firm, Demand theory, Supply theory, Price theory and Competitive theory. Further, the author opined that decision science bring tools and methods for decision analysis such as: Algebraic analysis, Optimization analysis, Forecasting analysis, Risk analysis and Discount and time-value-for-money analysis. More, the business functions and managerial economics areas are divided into variant units. These units are identified in solving management problems. They include: Production and operation, Marketing, Financing and Accounting and Human resource management.

Business Strategies Formulation

Strategy is the process that revolves around the decision of what will make up organizations' objectives, changes needed to be made, resources needed to be used, how it will be used, how the objective will be achieved and policies that will guide its achievement (Emeka, Ejim, and Amaka, 2015). Similarly, Drucker (1974) opined that business strategy is a wide program of activity designed by an organization to define how to achieve its goals as well as how to respond to the business environmental factors over time. Wilkinson (2005) added that this business function can be combined with economic theory and decision science in order to effectively utilize managerial economics activities. Furthermore, Jasapara and Divya (2016) maintained that managerial economics involves applying economic theory and quantitative methods (i.e. mathematics and statistics) to the management-related decision-making processes. It borders itself on questions like what is management more concerned with? Is management more concerned with company's market share? What specific condition can be applied to reach optimal solutions to management decision problems? Managerial economics deals with tools and techniques applied as an aid in solving problems that arise around the management corridor. Other tools that is applicable to management problems include SWOT analysis, Analytical Hierarchical Process (AHP), Return on Investment (ROI) analysis, Net

Present Value (NPV), Critical Path Analysis, etc. Managerial economics uses these managerial tools as aid to solving management problems. Business planning can be effectively done with comprehensive knowledge and understanding of microeconomic concepts and its applications. Optimum decision making to achieve the objective of the organisation which could either be for profit maximizing or for cost minimizing, is possible with proper application of microeconomic expertise, irrespective of the technological constraints and given market conditions. Microeconomic analysis is an imperative tool for solving practical day-to-day dilemmas and concerns (Juneja, 2018). Meier, Toole, Boyne, and Walker (2010) opined that strategies formulation is a guide to management in defining ends and means of a business. The same author stated that strategies formulation of organizations or firms begin with defining the firms' mission which is the unique purpose of business operation that differentiates it from another. Jasapara and Divya (2016) identified strategies formulation process to include:

Assessment of values, operations, philosophies, cultures, objectives: This includes checking values that the organization holds in esteem. Matching the strategy with the beliefs, culture and organizational norms.

Mission, Vision Concept: This stage expresses the organization's core purpose of existence. This helps in guiding and streamlining the activities of the organization over a period.

Environment Analysis: This helps organizations to understand and identify opportunities, threats, weakness and strengths. Environmental scanning covers the internal, external, macro and national environment of a business organization.

Laying Strategy Design: This includes specifying the major functions to be carrying out by the business, laying down specific approaches to be adopted in achieving firms' objective.

The resource based theory (RBT) emphases on firms' internal resources, and capabilities helps to explain the profit and value of the firm. It points out that differences between organizations occur because organizational resources are not equally distributed (Wernerfelt, 1984). The theory focus is on identifying valuable resources that aids firms to achieve sustainable competitive advantage and higher profitable returns. It posits that well-managed resources such as assets, capabilities, firm attributes, information, organizational processes and knowledge give firms the potential to create economic value (Barney, 1991). Similarly, Nwachukwu, Chlandkova, Fadeyi (2017) opined that resource based theory shows that the effective use of resources during strategies formulation could increase the firm's capacity to create new products, services, process and market expansion. In the context of managerial economics and strategies business formulation, the RBT could be applied in terms of ensuring that firms use the right managerial tools. Based on the propositions of the theory, the difference between firms' strategies formulation depends on the resources (skills, capabilities, knowledge, etc.) available. Hence, when these resources are well-managed, it results to effective and efficient business performance. Bordean, Borza, Rus And Mitra(2010) has outlined the business strategy process to involve the following steps: Analysis of the external and internal environment; Strategy formulation; Strategy implementation and Strategy evaluation

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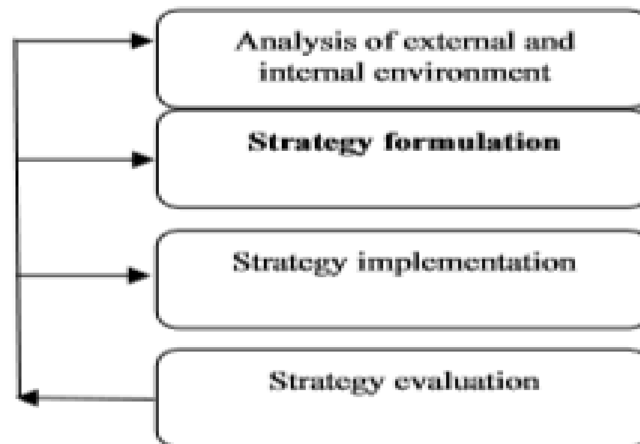

Figure1: Bordean, Borza, Rus And Mitra(2010) business strategy process

Managerial Economics AndBusiness Strategies Formulation Linkages

The various definitions of managerial economics have shown that the subject deals with the science of making management-related decision-making processes concerning the areas of Production and operation, Marketing ,Financing and Accounting and Human resource management. In developing business strategies, the focus is usually about making long time decisions that will affect the Profit maximization, Sales maximization, Increased market share/market dominance, Social/environmental concerns, Profit satisficing and Compete favourably. In designing the business strategy formulation, the core elements of the firm consisting of organization's mission, goals, and objectives and business activities that will enable it achieve set targets are brought together as the determining variables. These determining variables are used to set the organization's strategiespolicies byassessing the needs, values, and skills possessed by those who develop the strategy using a model developed by Alkhafaji, (2003) as shown below.

Figure-2: Strategy formulation model developed by Alkhafaji, (2003)

Discussion of Implications

Studies have found that strategies formulation is the bedrock for organizational success. The strategies formulation is a process that demands for tools that provide relevant information needed to plan, formulate policies and executive business strategies in order to achieve organizational goals and objectives. Supportively, Rajasekar (2014) found that a successful implementation determines the survival of a business and failure of the strategy's implementation will led to failure of business. Anna (2015) showed that there is a positive significant relationship between management tools and techniques including the effective use of firm resources. This implies that managerial economics relates with firms' strategies formulation in terms of allocation and control of firms' resources. Similarly, Indiatsu, Mwangi, &Mandere (2014) found that use of managerial economic tools boost firms' performance. The study shows that using tools like AHP (analytical hierarchy process), SWOT analysis, etc. will enhance business strategies formulation. For instance, AHP can help managers make decisions that involve choice making, ranking and prioritization, etc. Further, SWOT analysis enables managers to scan and evaluate their strength, weakness, opportunity and threat. Having relevant information, these elements will enable firms make well-informed decisions in terms of policy formulation, implementation and control, including consideration of strategies windows. Similarly, a study conducted by Iseri-Say, Toker, &Kantur, (2008) on over 25 set of managerial tools paid attention to how the acceptance of managerial tools influences organizational performance. The results revealed a significant positive relationship with competitive positioning, firm's integrity, functional capabilities, customer equity, and financial ratios. Efendioglu&Karabulut (2010) opined that managerial tools increase firms' performance as it aids decision making and evaluation of what has been made in order to achieve firms' set goals and objective. Hashim M. K. (2016) has recommended several methods of developing business strategies and a combination of these with managerial economics decision making model will be helpful in stringing the link between the business economics and strategies concepts. These methods of developing business strategies include the following:

a. Process vs. content approaches. This approach involves steps for identifying, selecting and implementing strategy based on information gathered from analyzing the strengths, weaknesses, opportunities, and threats facing the organization.This strategy will be helpful to managers in selecting low cost, differentiation or niche strategies for their products to help them maximize profits.

b. Economic vs. organizational approaches. Some managers view business strategy as a process that is very wide, complex and hence believe that effective business strategy cannot be formulated by using simpler approaches such as the process and content approaches. This approach recommend that the business strategy should focus on the parameters of The whole organization; The industry in which it operates; The competitive environment in which it competes; Long term direction; Organizational resources; The distinctive capabilities of the organization; and The prospect for success. Managers who combine managerial economics principles with this method find the strength to compete favourably with other manufacturers, increase their market share or diversify into new markets because of the knowledge the approach provides. This approach provides a long-time strategy formulation data to aid management information systems for the organization.

c. External vs. internal approaches. Managers are sometimes compelled to base their decisions onthe external and the internal controlling factors affecting their organization. While the external approach has a wider focus and scope,the internal focusses on its own distinctive capabilities. The external approach emphasizes environmental factors (such as political, economic, social, cultural, technology, ecology, government, legal, etc.) while the internal factors include analysis of the internal environmentsuch as resources, structure and culture. Managers of businesses while using this approach can identify external threats and opportunities that could affect their business either way. In the same token, they can define their business in terms of their strengths or what they can dobased on their internal resources, identify threats facing them and devise ways to combat these forces.

d. Prescriptive vs. descriptive approaches. This approach helps the manager to define in advance the various components of the strategy through an explicit, planned, and logical thought processes. This approach is based on the belief that different organizations in different business environments require different and not prescribed business strategies. The components for this approach include: Establishing the mission of an organization, Setting the objectives of the organization, Conducting the environmental scanning, Identifying the organization's internal strengths and weaknesses, Formulating alternative strategies, Choosing a strategy, Implementing the strategy and Evaluating and controlling the strategy. This strategy is of great importance to managerial leaders because the microeconomics and macroeconomics interplay of forces in one locality are different from others. In planning new product launches, entry to new market territories and determining the profitability of various market segments, this strategy is most compelling and useful in analyzing business data and making informed decisions.

e. Competitive advantage approach. This approach focuses on the firm's resources and distinctive capabilities as the basis for developing business strategy. The firm's competitive advantage includes resource, skill, activity or capability that are distinctive to those of the firm and may become the basis for competitive advantage. Business leaders in using this approach view the firmas a bundle of unique resources and capabilities whichare scare, durable, defensible or hard to imitate. They classify organizational resources as both tangible and intangible that include; physical assets, technology, information, human resources, financial resources, knowledge, skills, competencies, creativity, innovativeness, processes, functions, systems and intellectual properties. This provides a competitive edge over other firms in their drive for profitability and bigger market size.

f. The 3Cs approach. This approach emphasizes on the 3Cs (costs, customers and competition). The strategy is to focus on ways to lower operational costs, attract customers and overcome competition. Managers who base their decisions on this approach believe a company's competitiveness and growth normally resulted from the price/performance attributes of its current products, its ability to meet customer needs as well as pricing of goods or services lower than the competition.

g. Strategic thinking approach This approach helps managers to make more effective decisions by keeping and making them more alert of the threats and opportunities. By doing so, the strategic thinking approach helps them to formulate more effective strategy that can enhance their organizational performance. The aggregate implication of managerial economics as a tool for decision making can be traced to different aspects of business activities affecting decision on the price of a product and the quantity of the commodity to be

produced; deciding whether to manufacture a product or to buy from another manufacturer; choosing the production technique to be employed in the production of a given product; deciding on the level of inventory a firm will maintain of a product or raw material; deciding on the advertising media and the intensity of the advertising campaign; making employment and training decisions and making decisions regarding further business investment and the mode of financing the investment as earlier observed by Anandi P Sahu. It also facilitates other decisions such as demand and supply, marginal analysis, net present value and risk measurement. It helps in understanding the quantity of supply a firm could engage in over time, the marginal analysis as the tool makes it easier in analyzing business objectives like maximizing cost while present value tool aids managers to compare different cash flows that a manager can venture into at a period of time. The risk analysis helps in understanding several trade-offs that can be considered in business situations such as new product development, market expansion, outsourcing decisions, etc. in order to gain more benefits than losses.

Conclusion and Recommendation.

This study along with some previous ones have established that there exist an understanding and linkage between managerial economics and business strategies formulation in managing organisations in a successful manner, through well-informed decision-making processes. These decisions affect their market positioning, service rendition, products, asset and profit management. For these organisations and managers to remain competitive and profitable, eight different strategy formulation models have been discussed with far reaching implications for their business activities. The adoption of one or a combination of several of these models will provide the competitive edge required to win bigger market share and increase their profitability. There is further need to conduct the impact of these strategy formulation models using a business case study in order to identify the most appropriate in the Nigerian environment. Although the link between managerial economics and business strategies formulation has been established, the impact requires investigation and detailed evaluation.

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