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# Managerial Theories Of The Firm (Baumal's Theory Of Sales Revenue Maximisation):-

Managerial theories of the firm place emphasis on various incentive mechanisms in explaining the behaviour of managers and the implications of this conduct for their companies and the wider economy.
According to traditional theories, the firm is controlled by its owners and thus wishes to maximise short run profits. The more contemporary managerial theories of the firm examine the possibility that the firm is controlled not by its owners, but by its managers, and therefore does not aim to maximise profits. Although profit plays an important role in these theories as well, it is no longer seen as the sole or dominating goal of the firm. The other possible aims might be sales revenue maximisation or growth.

## Baumol's Theory of Sales Revenue Maximisation

According to theory, once profits reach acceptable levels, the goal of the firms become maximisation of sales revenue rather than maximisation of profits. In the words of Baumoul, 'The sales maximisation goal says that managers of firms seek to maximise their sales revenue subject to the constraint of earning a satisfactory

profits. "
The above definition maintains that when the profits of firms reach a level considered satisfactory by the shareholders then the efforts of the managers are directed to maximise revenue by promoting sales instead of maximising profit. While studying this theory. K must be kept in view that firms do not Ignore profit altogether. They do aspire to attain a general level of profit. But once an acceptable level of profit is obtained their goal shifts to sales maximisation in place of profit maximisation.
Baumol raised serious questions on the validity of profit maximisation as an objective of the firm. He stressed that in competitive markets, firms would rather aim at maximising revenue, through maximisation of sales. According to him, sales volumes, and not profit volumes, determine market leadership in competition. He further stressed that in large organisations, management is separate from owners. Hence there would always be a dichotomy of managers' goals and owners' goals. Manager's salary and other benefits are largely linked with sales volumes, rather than profits.
Baumol hypothesised that managers often attach their personal prestige to the company's revenue or sales; therefore they would rather attempt to maximise the firm's total revenue, instead of profits. Moreover, sales volumes are better indicator of firm's position in the market, and growing sales strengthen the competitive spirit of the firm. Since operations of the firm are in the hands of

managers, and managers' performance is measured in terms of achieving sales targets, therefore it follows that management is more interested in maximising sales, with a constraint of minimum profit. Hence the objective is not to maximise profit, but to maximise sales revenue, along with which, firms need to maintain a minimum level of profit to keep shareholder satisfied. This minimum level of profit is regarded as the profit constraint.

However, empirical evidence to support above arguments of Baumol is not sufficient to draw any definite conclusion. Whatever research has been done is based on inadequate data; hence the results are inconclusive.